Division of Agricultural Sciences

UNIVERSITY OF CALIFORNIA

Membership Marketing Contracts of Agricultural Cooperatives in California

W. F. Mueller
J. M. Tinley

CALIFORNIA AGRICULTURAL EXPERIMENT STATION

BULLETIN 760

What are the economic functions of marketing contracts?

What kind of contract should a coöperative use?

Should the contract run for only a year, or longer?

What is a fitting penalty for nonperformance?

How much integration is desirable?

The marketing contracts used today by California agricultural coöperatives reveal a wide choice of answers to these and many other related questions. Contract provisions differ not only among associations handling different kinds of products but also among those handling the same commodities.

To find out what makes a good marketing contract, the authors have drawn on the experience of more than 200 agricultural marketing coöperatives in California. Their analysis of existing contracts and bylaws makes clear why there can be no single, ideal contract that will fit all marketing associations. In a discussion of the economic and legal functions of contracts, the authors raise the important points that each association should consider—in relation to its particular needs—in order to develop a satisfactory contract for its members.

This bulletin should be useful both to new coöperatives working out their first marketing contracts and to established associations seeking to improve existing contracts.

THE AUTHORS:

W. F. Mueller was, during the preparation of this bulletin, Assistant Professor of Agricultural Economics and Assistant Agricultural Economist in the Experiment Station and on the Giannini Foundation, Davis.

J. M. Tinley is Professor of Agricultural Economics and Agricultural Economist in the Experiment Station and on the Giannini Foundation, Davis.

MARCH, 1958

MEMBERSHIP MARKETING CONTRACTS of AGRICULTURAL COOPERATIVES in CALIFORNIA[1]

W. F. MUELLER

J. M. TINLEY

I. WHAT MAKES A GOOD COOPERATIVE MARKETING CONTRACT?

The marketing contract is *one* of the tools available to those wishing to build a successful coöperative. It is by no means the only tool needed for successful coöperation, but it is an important one. Because marketing problems and objectives may vary widely from one association to another, each coöperative should choose contract provisions best suited to its particular needs.

Although the historical origins, marketing functions, and commodity peculiarities of each association tend to make its needs unique, we can make certain generalizations about what a good coöperative marketing contract is. We can at least help the coöperative by framing the questions that it should answer in developing a contract that will be good for its particular needs.

Forms of Contracts

The marketing contract may be included in the bylaws of a coöperative, or it may be a separate legal document. Legally, there is no difference between these forms. In regard to clarity and convenience, however, there are important differences.

A separate document seems more appropriate. One advantage is that it clearly isolates all the marketing obligations and rights of both parties from other aspects of the bylaws. Another is that putting all the marketing provisions in a separate document makes it possible to spell them out in greater detail, leaving little doubt as to what is expected of each party in relation to marketing. Moreover, an association that also does business

> Questions that each coöperative should put to itself to determine how much integration is desirable for its members and to develop a satisfactory marketing contract are given at the end of this section. These questions also provide a guide to the contents of this publication, as page numbers have been included for quick reference to discussion of the various points an association should consider in working out its own particular set of answers.

[1] Submitted for publication April 11, 1957.

with nonmembers must use a separate contract for them, since the association cannot make them sign the bylaws, which apply only to members.

Language of Contracts

For the layman, coöperative marketing contracts should be as understandable and as unambiguous as possible. Lawyers, like economists, are not generally applauded for their literary clarity. But legal documents can and should be made readable for the layman as well as the lawyer. Many California coöperatives have succeeded in this respect. The terms of their contracts are spelled out clearly, and they are also organized to make for easy reading.

Some contracts are made more readable by the use of side or marginal headings for the various provisions. The reader can thus readily find clauses of particular interest. For example, some of the marginal headings used by a fruit association are: "sale and delivery of products," "duration of membership agreement," "disposition and handling by association," "arbitration of disputes as to grades," "liquidated damages for nondelivery," "home canning," "crop reports," "notices," and "bona fide transfers." Such headings are especially helpful in very long contracts.

A final aid to more readable contracts is the avoidance of very small print. While small print may make a long contract appear shorter than it actually is, it also proves a strong deterrent to close reading by members.

Contract Provisions

It is most important from an operational standpoint that marketing contracts include the appropriate provisions. Such appropriateness can be measured in two ways, legally and economically. Legally, the appropriateness of a marketing contract depends mostly on whether it is an enforceable document. Economically, its appropriateness is determined by whether it best accomplishes the economic objectives of the association.

The legal aspect. We shall not explain here what a legally desirable contract is. Any good coöperative counsel can see to this. But care should be taken to aid such counsels in regard to the economically appropriate provisions that should be included. Many lawyers may not be familiar with all the operational peculiarities and economic objectives of the coöperatives they represent. They may, therefore, tend to pattern coöperative marketing contracts after those of noncoöperatives, which often deal almost exclusively with delivery, sale, or agency provisions, and overlook some of the other important integrating features needed in coöperative contracts. This may leave some of the integrating practices of coöperatives without a sound and workable legal basis.

This problem can best be overcome if coöperative management fully informs its lawyers about its operations. The attorney can then decide if certain practices should be given a legal basis in the association's marketing contract.

The economic aspect. If coöperatives are to operate most efficiently, certain production and marketing activities of farmers must be closely integrated with their association. The marketing contract provides the legal basis of such integration. It spells out the duties and rights of both parties relative to certain marketing decisions. For example, it may give the association the right to make decisions concerning the time individual members should harvest their crops.

Before an association can decide upon the economic appropriateness of particular contract provisions, it must evaluate its own economic objectives. It must decide how it wishes to qualify the basic economic objective of increasing its members' farm income. Most associations will qualify this objective somewhat. More important, American farm-

ers are not willing to surrender all of their production and marketing decisions to their association. But most farmers are willing to give up some of their decision-making power to the association in the interest of greater economic returns.

Thus, there may be a basic conflict between an association's desire for economic efficiency—which may require close integration—and the rights and wishes of its individual members. Each farmer faces this conflict, and many will look at it differently. Some will be willing to give up more freedom than others.

Fortunately, coöperatives are seldom confronted with "all-or-nothing" propositions. Seldom does deviation from the economically optimum position lead to disastrous inefficiency. There are as many shades of economic efficiency as of individual freedom. Fortunately again, in our democratic society it is for the individuals forming a coöperative to decide how to reconcile the conflict between collective or group economic efficiency and individual managerial freedom. (Of course coöperative members cannot exercise complete freedom in this respect. They can not, for example, bind themselves together in such a way as to constitute a monoply in violation of the country's antitrust laws.)

Since this conflict can only be resolved ultimately by a coöperative and its associated membership, there is no single, clear-cut answer that can be provided here. The conflict can be resolved more easily and satisfactorily, however, if the association asks itself the proper questions. Such questions are raised and discussed throughout this study. The question of how much integration is desirable is dealt with on pages 49–50. The question of contract length is discussed on pages 19–21, and the proper size of liquidated damages on pages 27–33. Below are important questions concerning matters which a coöperative may consider including in its marketing contract.

1. *Delivery and acceptance.* How much of their crop should members be obligated to deliver? How much should they be permitted to retain for home use? How much of its patrons' crops should the association be obligated to accept? Should the association be permitted to decline acceptance, and its patrons to refuse delivery, under certain special circumstances? Should the contract provide for prorating acceptance in some equitable manner in the event of forced limited acceptance? (See pages 35–39.)

2. *Time and place of delivery.* Should the association be permitted to set the delivery time and place? Should members be required to deliver their entire crop before some specified date? (See page 41.)

3. *Method of payment.* When should patrons be paid? Should their association be permitted to set up a grading system to be used in paying its members? Should arbitration be provided for in the event of disagreement over interpretation of such a grading system? (See page 47.)

4. *Termination of contracts.* How long should the contract run? How should members be permitted to terminate their contracts? How may members who have left the association or been expelled from it be permitted to rejoin? (See page 47.)

5. *Enforcement methods.* Should the contract specify the extent of liquidated damages? How large should these damages be? Should they be a fixed absolute amount or a fixed percentage of the product's market value? Should minimum damages be prescribed? (See page 27.)

6. *Crop inspection and reporting.* Should the association be permitted to inspect certain of its members' farming operations? Should patrons be required to notify the association of changes in acreage and of expected crop yields? (See pages 42–43.)

7. *Quality requirements.* Should the association be permitted to set quality standards which its members must meet

to retain their membership? How should such standards be enforced—by expulsion for noncompliance or by assessment of damages? (See pages 39–40.)

8. *Crop harvesting.* Should the association be permitted to set harvest provisions or be authorized to perform the actual harvest? (See page 40.)

9. *Crop pooling.* Should the association be authorized to pool its members' crops? (See page 42.)

10. *Independence of control.* Should the association's management be free to function independent of interference from individual members? (See pages 43–44.)

11. *Industry marketing agreements.* Should members give their association's directors the right to vote for them in a marketing agreement referendum? (See pages 45–46.)

12. *Method of operation.* Should the marketing contract specify that the association follow the principle of cost operation and of equal treatment of all patrons? (See pages 44–45.)

13. *Processing coöperative is to perform.* Should the association undertake to process patrons' crops into certain products? (See page 45.)

14. *Transfer of obligation.* Should the coöperative permit its patrons to transfer their obligation to perform on their contracts? Under what conditions should such transfers be permitted—only on death? (See page 48.)

15. *Litigation costs.* Should the contract specify that in litigation over breach of contract, the party losing such actions should pay the other's litigation costs? (See page 34.)

16. *Guarantee of control.* Should the contract specify that the patron has complete control over the crops he contracts to deliver? (See page 48.)

II. INTRODUCTION

This study emerged during the course of two long-term research projects related to the economic and financial aspects of agricultural marketing and purchasing coöperatives in California—one concerned with the methods such coöperatives use to finance their operations, the other with the problems of integration within and between coöperatives. Basic information was collected by means of questionnaires sent to all marketing and purchasing coöperatives in the state and by personal visits to many of them. All those visited and a considerable number of those that returned questionnaires supplied copies of their articles of incorporation, their bylaws, and their marketing contracts with members.

Since the contractual relations between members and their coöperative associations are intimately related to the problems of both financing and integration, it was decided to make the special analysis of membership marketing contracts that is presented here. This publication may thus be regarded as an integral part of the two broader long-term studies.

Marketing contracts are also known as marketing agreements and membership contracts. The authors prefer the term "marketing contracts" because today the term "marketing agreement" is commonly used to describe the industry-wide marketing agreements operating under the Agricultural Marketing Act of 1937 and various similar state laws. In practice, however, many coöperatives use this term, especially when the contracts are separate from the bylaws. The term "membership contracts" is seldom used today to describe marketing contracts; it generally refers to the contract a member signs upon joining an association, which states that the member ratifies and

adopts the association's articles of incorporation and bylaws. In most cases, acceptance of the bylaws may also involve acceptance of the coöperative marketing contract.

Economic Importance of Agricultural Coöperatives

In 1954–55 there were 9,887 agricultural coöperative associations in the United States engaged in marketing farm products, purchasing farm supplies for members, or rendering some form of marketing service (Gessner, 1957).[2] These associations had a combined membership of some 7,600,000 (many farmers belong to two or more) and in 1953–54 transacted a gross volume of business amounting to $12.5 billion, of which $9.3 billion was from the sale of farm products, $2.9 billion for farm supplies handled, and $195 million for marketing services rendered. The average gross volume of business per association was thus about $1,264,000.

The 454 agricultural marketing, supply, and service coöperatives in California had a combined membership of only 121,600 or 1.6 per cent of the total for the United States. The California coöperatives, however, had a gross volume of business of almost $1.2 billion or about 9.5 per cent of the combined volume for the United States.[3] In California the average volume of business per association was $2,614,000 as compared with the national average of $1,264,000 per association. Similarly, the gross volume of business transacted per member by the 454 California coöperatives was $9,800 as compared with a national average of $1,600 per member. Although the majority of the 454 marketing, supply, and service coöperatives may be classified as local associations (i.e., associations operating in a restricted area), more than 20 are either large centralized associations (i.e., they operate over the whole state or a large part of it) or federated associations (i.e., an affiliation of several local associations). Financial reports available from most of the large federated and centralized associations indicate that many of them have a gross volume of business in excess of $25 million a year. Individual farmers who are members of coöperative marketing, supply, and service organizations have contributed many millions of dollars to supply the capital needed by their associations.

In view of these facts it is no wonder that in California there has grown up over the years a rather highly formalized contractual relationship between individual members and their associations—embodied either in the bylaws or in separate marketing agreements or contracts. It has also been known that there are significant variations in the details of these contracts as between associations handling the same types of products (citrus fruit, for example) as well as between associations handling different types of products or performing different types of service. It is the purpose of this study to analyze these differences in some detail.

Recent advances in the economic theory of coöperation, particularly those made by Ivan V. Emelianoff, Frank Robotka, and Richard Phillips (Phillips, 1952), should prove helpful in this analysis. They will help us make more meaningful hypotheses about the reasons for and implications of various contract provisions.

[2] See "Literature Cited" for citations, referred to in the text by author and date.

[3] The net value of business of coöperative associations in California was $829 million. This figure represents the volume of business transacted by local and centralized associations. In other words, it excludes the value of business transacted by federated coöperatives from the gross value on behalf of local member cooperatives.

III. ORIGIN AND MEANING OF THE MARKETING CONTRACT

The Agricultural Coöperative Association

We can best understand the nature and function of coöperative marketing contracts by first getting a clear understanding of the economic nature and function of agricultural coöperative marketing associations.

Agricultural coöperatives as a way of doing business may have social as well as economic bases, but in the United States, especially in recent times, their basic objectives or goals have been economic. Farmers have resorted to this means of business to improve their economic position in a capitalistic economy.

Relatively few farming enterprises in the United States are large enough to justify extending their economic activities into the processing and marketing of the commodities they produce. To do so, the farmer would have to own and control the facilities and equipment necessary for processing and marketing as well as those needed for production. Such ownership and operation of successive stages of production and marketing is known as *vertical integration.* The great majority of farms in the United States are too small to permit such integration individually. However, by associating with others to form a coöperative corporation, farmers have been able to extend their operations beyond the farm—into the economic activities of processing and marketing.

Such multiple-stage production and marketing operations are becoming increasingly common in our complex modern economy. For a variety of reasons, many types of business find it more economical to extend their activities into several stages of production and distribution. In the petroleum industry, many companies own their own wells, refineries, pipelines, and retail outlets. Steel companies often own their own mines as well as manufacturing plants. And agricultural processing concerns sometimes integrate backward into agricultural production as well as forward into several stages of distribution.

Similarly, when a number of farmers unite in joint ownership of agricultural marketing and processing facilities, it is simply a form of vertical integration. For while the coöperative organization enjoys certain rights apart from its individual owner-patrons (due to its incorporation as a legal entity), it exists for, and is ultimately controlled by, them. In truth, the economic relationship between farmers and their jointly owned associations often is like—both economically and legally—the vertical integration involved when several industrial firms form jointly owned subsidiary companies. Such jointly owned companies are operated for the benefit of their legal parents. For example, several railroad companies often own jointly terminal facilities and railroad bridges. Retail grocers frequently combine to form jointly owned associations to act as their buying agents. Chemical companies also often have united to form jointly owned subsidiary companies, both in domestic and foreign markets. The reason is usually that business firms can often perform a task better through joint action than through individual action.

There are two main economic differences between agricultural coöperatives and most other forms of vertical integration[4] found in our economy.

---

[4] Strictly speaking, vertical integration is only one form of "vertical extension," the latter being defined as the "extension of the scope of an enterprise so that it influences more processes between raw material extraction and the final sale of the finished product. . . . Vertical integration thus is one form of vertical extension and consists of extending a firm's scope vertically through ownership." (Alfred R. Oxenfelt, *Industrial Price and Market Practices;* New York: Prentice Hall, 1951, p. 207.) Thus, narrowly, vertical integration occurs only between owner-patrons and their coöperative.

First, because farm firms are relatively small, a large number must join together when they integrate. This is not usually true of most industrial concerns. Practically all are large enough (or can become large enough) to integrate forward or backward individually. And even when one concern is not large enough to do a job for itself, it usually need join with only one or two other firms to undertake an efficient jointly owned operation.

Second, agricultural coöperatives usually operate their jointly owned facilities entirely for the benefit of their patron-owners (and occasionally of their nonowner patrons) on a patronage rather than an ownership basis. Many nonagricultural concerns operating jointly owned subsidiaries also follow this procedure, but the practice has become so universally accepted by agricultural coöperatives that it might properly be considered their foremost distinguishing characteristic. Of course, insofar as patronage is proportional to ownership, as is increasingly common in California coöperatives, there is no distinction between the two.

The Economic Function of Coöperative Marketing Contracts

Successful vertical integration (that is, aiming at maximizing members' incomes) through coöperation requires that certain activities of members and their coöperatives be integrated or coördinated. Insofar as farmers have other goals of coöperation, some of the following discussion of the methods coöperatives should use to achieve this profit end may not be relevant; but even coöperatives motivated by noneconomic considerations must operate at something approaching maximum economic efficiency to survive in a competitive world.

When farmers join or form coöperatives to further their individual economic positions, they must also be willing to surrender some of their individual sovereignty to the association, for only in this way can the coöperative be run as an efficient economic extension of its members' individual farm firms. Formally, individual members make concessions to their coöperative, but in reality they make concessions to its owners, that is, its other member-patrons. This involves multilateral agreements between all members.[5] It is well to keep this in mind. Treating the coöperative as an entity apart from its members may result in serious analytical pitfalls. An especially important feature of such integration is the continuing participation of patrons in their association.

The association's facilities are built and its management is hired to serve its patrons. In carrying out its buying, processing, storing, selling, and other functions, the coöperative (as the representative of all members) may make large capital investments. In making them, it usually borrows the necessary funds from its members or elsewhere. Many such investments are of fixed character—once made, their total cost varies but

The relationship between nonowner patrons and a coöperative involves different forms of vertical extension. It may be based entirely upon the patron's voluntary participation in the coöperative. But when nonowner patrons are tied to the coöperative by the same marketing contracts as members and are treated the same as members with respect to patronage dividends and in other important respects, their vertical extension may be as complete as between owner-patrons and their coöperative. The most important difference, of course, is that nonowner patrons generally have no formal voice over the coöperative's policy. In practice, this difference may be more imagined than real.

[5] Phillips (1952, pp. 63–64) explains the agreements between members as follows: "This multilateral agreement is a formal one—ordinarily a binding contract between sovereign and otherwise independent firms. This formal agreement does not alter the entrepreneurial decision-making body—that function continues to rest with the individual firms. It does, however, involve coordination of the activities and functions of the decision-making units with respect to the joint plant."

little with the volume of plant operations. In making these fixed investments, a coöperative must make certain estimates about its future business volume. Should these estimates prove wrong, the coöperative, and eventually its member patrons, may suffer serious losses.

One cause for uncertainty about the future is patron "disloyalty." Without some legal or nonlegal means of assuring continued patron participation, coöperation is a very loose form of vertical integration. It is then based solely on the voluntary participation of its patrons, who may break or renew their membership at will. The bond between a farmer and his coöperative is tied by nothing stronger than membership loyalty, good will, or whim.

Under such circumstances, the disloyalty of a minority of patrons may seriously jeopardize the economic interests of the remainder. Because many costs are fixed, average unit costs depend primarily on business volume. Therefore, when some patrons temporarily are tempted to sell outside their association, those patrons continuing to sell through it will likely receive lower net returns than those selling outside it. To have their loyalty repaid in this way may encourage additional members to sell outside the association in subsequent years. Thus, what may have started as the temporary disloyalty of a few members may shortly snowball until the association is ruined. This danger is especially real in the early years of a new coöperative when it needs time to prove itself, to assemble and train personnel, and to eliminate "squeaks and rattles." During this "shakedown" period coöperatives may be easy prey to strong rivals seeking to crush them by temporarily paying higher prices to some coöperative members. Marketing contracts are one means of protecting a coöperative association against such actions (other factors are discussed on pages 24–26). They may require farmers to market through their association for a specified period.

Some economists have cited other advantages of coöperative marketing contracts, but, for the most part, these are simply variations of the reason given above. For example, Bakken and Schaars (1937, pp. 307–312) point out that marketing contracts (1) assure the association the continuous support of its members; (2) cut down the cost of assembling members' products by insuring their delivery; (3) assure the association a certain volume of business upon which to plan future operations, sales, commitments, and merchandising programs; (4) permit an association to adjust its costs to a minimum; (5) assist the association in its financing operations; and (6) enhance the prestige of the association. These are all valid justifications for marketing contracts, but all are reducible to the same fundamental advantage: marketing contracts provide such integration of patron and coöperative activity as to insure that the coöperative will have a definite volume of business during a particular period. And by reducing uncertainty in this respect, an association can operate more efficiently in making both short- and long-run investment and other decisions.

Advantages to operating efficiency resulting from stabilizing business volume are not peculiar to coöperatives. Noncooperative concerns, recognizing this problem, have made increasing use of marketing contracts to insure themselves a more uniform volume of business. It is because farmers anticipate receiving higher returns by selling through cooperatives that they are willing to enter into marketing contracts with them. Because a particular noncoöperative marketing concern generally cannot promise a farmer higher prices than the general market price, there is little economic incentive for a farmer to make agreements with them unless nonprice advantages are anticipated. Of course, where buyers are few, farmers often find it desirable

to enter into marketing contracts with them to make certain that they will have a market for their product. In these circumstances, buyers often must state at the beginning of the planting season a specific or minimum price in their marketing contracts to induce enough growers to make such contracts with them.

Because of this difference in farmers' attitudes toward coöperative and noncooperative marketing agencies, it seems proper to conclude that coöperatives may have a definite advantage in the use of marketing contracts. Other things being the same, coöperatives are better able to use marketing contracts in stabilizing their volume of business than are noncooperative concerns. This is not to imply that coöperatives may not stabilize their volume of business at too low a level. But when this happens, it is not ordinarily the fault of marketing contracts as such, although, as pointed out below, unduly lengthy contracts may restrict membership in coöperatives.

Like Bakken and Schaars, other students of coöperation have looked at only the integrating feature of coöperative marketing contracts discussed above (Steen, 1923, pp. 312–15; Jesness, 1932, pp. 185–86; Nourse, 1927, pp. 171–77). It is true that the "maintenance clause" feature of marketing contracts is always important and apparently was the only important feature of early contracts. But today it is by no means the only important integrating feature of coöperative marketing contracts. Through the years, coöperative managers and directors increasingly have recognized the need for closer integration between growers and their coöperatives in other respects. Not only must performance be assured, but the time, place, and manner of performance are often important also. At times the coöperative must also be able to control the quality of individual members' production. Sometimes most efficient operation requires not complete performance but limited performance. To insure the degree of integration necessary to achieve maximum operating efficiency, the legal rights and duties of patrons under the above circumstances must be spelled out in the marketing contract. More and more coöperatives have done just this.

The term "marketing contracts" as used herein means *the legal basis integrating certain marketing relationships between patrons and their association.*

The Development of Marketing Contracts

Coöperatives have used marketing contracts as a legal integrating device for over half a century. Apparently the Swiss, and later the Danes, were the first to use them. In the latter half of the nineteenth century, Danish coöperative creamery and bacon-selling associations began using marketing contracts (Steen, 1923, p. 30). These associations initially had depended entirely on the mutual respect, good will, and loyalty of their members to insure their continued participation. But successive experiences with disloyalty of members, tempted by temporarily higher prices of noncoöperative dealers, contributed to many coöperative failures. To prevent such raids on their membership, the Danish associations reinforced member loyalty with legal obligations to market through the associations for a specified period. This marked the beginning of coöperative marketing contracts which have remained a common feature of coöperation in Denmark to the present day.

As far as can be ascertained, the first American coöperative to use a marketing contract was a farmers' elevator in Iowa. In 1889 it adopted a contract which permitted members to sell elsewhere only upon payment of a penalty of one cent a bushel (Steen, 1923, p. 310).

The adoption of coöperative marketing contracts by early American associations probably involved an evolution similar to that of the Danish association

but separate from it. However, the Danes' successful experiments with contracts may have influenced some early American agricultural coöperatives. In the early 1890's orange growers in southern California began signing marketing contracts with their associations. One authority claims these early contracts were copied directly from the Danes (Steen, 1923, pp. 310–311). Another reports that these early associations may have been encouraged to use such contracts because noncoöperative citrus buyers used them (MacCurdy, 1925, p. 22). Other California coöperatives followed the example of the early citrus associations.

Since the turn of the century, and especially since 1910, marketing contracts have become common in practically every field of coöperative marketing. As early as 1923, of 185 associations larger than county-wide in scope, over 160 used marketing contracts (Steen, 1923).

While marketing contracts gained increasing acceptance through the years, their forms and objectives have changed. Most of the early contracts were of short duration. They usually bound growers to sell through their association for but a single marketing season. For example, while the early California citrus contracts were for 21 years, they could be cancelled by either party annually. Similarly, the contracts between the California Fruit Growers Exchange and its local associations were for 20 years, but the locals were given the option of withdrawing on September 1 of any year by giving proper written notice.

After 1920, marketing contracts for longer periods became common throughout the United States. Many coöperatives formed during the twenties were centralized associations with five-year marketing contracts. The avowed purpose of many of them was to gain control over the supply of particular agricultural products and to use such control to enhance prices. To accomplish this end, these associations felt obligated to bind their members for more than a single year.

But in spite of their long-term, "ironclad" contracts, practically none of the associations using them were able to prevent membership nonperformance; they either failed, or they were forced to modify their operations and liberalize their contracts (Hood, 1927, pp. 287–293). The failure of these associations was not caused by the nature of their marketing contracts. It would be more correct to say that they failed in spite of them. The chief reason for failure was their inability to control the supply, not only of nonmember production but of their members as well. This made monopolization impossible.

Since the late 1920's long-term contracts without annual withdrawal privilege have become increasingly less common. Bakken and Schaars' (1937, p. 320) study of 83 large-scale American coöperative sales associations in 1934–35 indicated that more than half had contracts of three years or less. But at that time one out of four of these associations still had contracts of ten or more years' duration.

IV. LEGAL NATURE OF THE CONTRACT

The coöperative marketing contract is a legal document. Without recourse to legal remedy, it would be practically worthless. It would simply be a written pledge depending solely on a moral obligation to fellow coöperators. When coöperatives began using marketing contracts, around 1900, the courts often questioned their legality as means of enforcing members' sale through their association. By the early 1920's, however, the courts in most states accepted them as a legitimate means of controlling membership participation. Nourse (1927, pp. 282–3) summarizes the three grounds upon which the courts relied in accepting

the contract method of tying a coöperative together as follows:

(1) That it is proper that a mutual association provide for the financing of its current operations by the assessment of their cost upon the whole body of members, who themselves adopt this provision as one feature of their by-laws; (2) That an association making capital outlays for the erection of buildings or otherwise must make definite contract arrangement for the liquidation of such long-term obligations by equitable distribution of the burden over the membership who are to be benefited by such outlays and will be the owners of the property; and

(3) That the purposes of the association in providing more efficient or more economical processing or marketing services can be realized only if mutually supported by a sufficiently large number of people on a sufficiently permanent basis.

While the courts have since continued to find coöperative marketing contracts legal on these grounds, such contracts may be declared illegal unless they include certain safeguards for both parties. Basic to the legality of all contracts is the concept of mutuality. This means that both parties to a contract must be bound by it. To insure that a contract possesses such mutuality of duties and rights, it should be in writing, setting forth clearly and fully the rights and duties of both parties (Hulbert, 1942, p. 115).

Another important determinant of the legality of coöperative marketing contracts is the amount which members agree to pay for nonperformance. The liquidated damages provisions of contracts are legal if the specified damages do not greatly exceed the actual losses suffered by the association due to nondelivery. If they greatly exceed actual damages, the courts may declare them illegal because they involve "penalties" rather than "damages" (Packel, 1947, pp. 154–55). For this reason coöperatives must keep the stated amounts of such damages within reason.

Another common provision determining the legality of marketing contracts is their duration. Coöperative marketing statutes in most states restrict the maximum period that such contracts may run. The California law restricts this period to 15 years.[6] While contracts may not run for longer than the periods specified in the various states, the courts have held that a contract may run continuously if an annual withdrawal privilege is included (Hulbert, 1942, pp. 130–31). Such a "continuous" contract is in effect, a one-year contract with the provision for automatic renewal unless an action is taken by a member or the association to discontinue it. As noted below, most coöperative marketing contracts in California are now of this form.

Legal Remedies for Nonperformance

A coöperative uses marketing contracts because they give it a legal means of forcing members to keep their promise to do business through it, or to compensate it if they fail to do so. The legal remedies available to coöperatives when a marketing contract is broken are the same as those applying to other contracts involving persons or businesses. In addition, the California law provides that coöperative associations whose marketing contracts are broken may, if the contracts so specify, be entitled to the remedy of liquidated damages and, even though not specified, to remedies of specific performance and injunction.

Liquidated damages is a form of legal relief whereby the party breaking the contract may be compelled to pay the other party to the contract a specified amount agreed to in advance, without the necessity of the aggrieved party being compelled to prove the amount of actual damage suffered. The injured party needs only to prove that a breach of contract has occurred. Unlike specific performance and injunction, liquidated damages can be assessed directly by an association without recourse to the courts. Even in the case of liquidated damages, however,

[6] Agricultural Code of California (Revised Sept. 15, 1945), Section 1208.

it may be necessary for an association to seek court sanction if a member refuses to pay and if he has no assets in the association which can be debited or drawn on.

Section 1209 of the California Agricultural Code states:

> The by-laws or the marketing contract may fix as liquidated damages, specific sums to be paid by the member or stockholder to the association upon the breach by him of any provision of the marketing contract regarding the sale or delivery or withholding of products; and may further provide that the member will pay all costs, premiums for bonds, expenses and fees in case any action is brought upon the contract by the association, and any such provisions shall be valid and enforceable in the courts of this State; and such clauses providing for liquidated damages shall be enforceable as such and shall not be regarded as penalties.

The right to recover actual damages in the event of a breach of contract is available even though there is no provision for liquidated damages. This requires specific and detailed proof of the actual damage suffered. In many cases it is extremely difficult, and often impossible, to establish accurately the damage actually suffered, and experience has taught coöperatives that it is desirable to specify in their marketing contracts an agreed amount as liquidated damages rather than rely on the right to recover actual damages. If the amount specified is not greatly in excess of the possible actual damages suffered, the damages specified are legal.

Spelling out the extent of damages in the marketing contract has more than a legal advantage. By doing so, a member anticipating breaking a contract knows exactly what it will cost him to do so. Because both parties know just what to expect in the event a contract is broken, an association can usually collect such damages without bringing a legal action. As a result, membership ill will may be kept to a minimum. In fact, it is not uncommon for a member to break a contract one year, pay the association his liquidated damages, and remain a member in good standing. There have been cases when noncoöperative concerns have engaged in price wars, where coöperative management has urged members to sell on the outside and pay their damages to the association. This action usually results in a quick cessation of the price war.

As was pointed out above, if liquidated damages are not specified in the contract, it is necessary to turn to the courts to arrive at the amount of actual damages. Such action may result in serious membership antagonism, often causing members to leave the association when their contracts expire.

If liquidated damages do not provide adequate relief to an association, it may ask the court for a decree of specific performance. Such a decree involves an action by the court, ordering the member who is breaking, or is threatening to break, a contract to carry it out. Failure of a member to comply with the court's decree results in a citation for contempt of court, for which he may be fined and/or imprisoned.

Whereas liquidated damages and specific performance are positive legal remedies, injunctions afford a negative remedy. An injunction granted under a marketing contract is an order by the court restraining the offending party from selling his crop outside of the association. A party disobeying an injunction is held to be in contempt of court and is punishable by fines and imprisonment. Section 1210 of the California Agricultural Code reads:

> In the event of any such breach or threatened breach of such marketing contract by a member, the association shall be entitled to an injunction to prevent the further breach of the contract and to a decree of specific performance thereof. Pending the adjudication of such an action and upon filing a verified complaint showing the breach or threatened breach, and upon filing a sufficient bond, the association shall be entitled to a temporary restraining order and preliminary injunction against the member.

Injunctions may also be used against individuals not parties to the contract in question. For example, if a third party encourages coöperative members to break their contracts, the association may obtain a court injunction ordering him to discontinue such activities. Failure to abide by such an order may result in punishment for contempt of court. In California such injunction against third parties can be obtained only if copies of the contract are filed in the county courthouse.

Although all these remedies are available to associations in enforcing their marketing contracts, liquidated damages are most commonly used today. Most coöperatives spell out clearly the extent of such damages in their contracts both to insure their legality and to improve membership relations.

V. CALIFORNIA EXPERIENCE

How Many Coöperatives Use Marketing Contracts?

The preceding discussion has outlined the general economic and legal nature of coöperative marketing contracts, and has dealt briefly with their historical origin and development. Let us now examine their current nature and function. To accomplish this we shall describe and analyze the legal form, duration, enforcement provisions, integrating provisions, and other features of contemporary California contracts. Much of the data pre-

Table 1. Number of California Coöperatives Using Marketing Contracts, by Commodities

Type of association	Total number coöperatives		Coöperatives with contracts		Coöperatives without contracts	
	In sample	Estimated no. in state*	In sample	Estimated no. in state†	In sample	Estimated no. in state†
Citrus	61	173	61	173	0	0
Wine	17	28	17	28	0	0
Other fruits and vegetables	65	131	57	115	8	16
Nuts	23	26	23	26	0	0
Dairy	13	28	9	19	4	9
Livestock	2	6	0	0	2	6
Field crops	25	40	24	38	1‡	2
Poultry	9	22	7	17	2§	5
Purchasing	8	17	1	2	7	15
Miscellaneous	5	6	4	5	1	1
Total	228	477	203	423	25	54

* These are the coöperatives to which we sent questionnaires and which we assumed to be still in business.

† These estimates are made on the assumption that the percentage of all coöperatives of each product type using contracts is the same as that of the sample. For example, 9 (69 per cent) of the 13 dairy coöperatives in our sample use contracts. If we assume that 69 per cent of all 28 dairy coöperatives in the state use contracts, then 19 use contracts and 9 do not. We have weighted our samples for each type of association in this way. This results in a more accurate estimate of state figures because there generally is less variation within commodity groups than between groups. For example, all of 61 citrus associations in our sample use contracts. On the other hand, only one of the eight purchasing associations in our sample uses a marketing contract. The reliability of these estimates and those in tables 2 and 3 varies from one product to another, depending on the size of the samples and the total population.

‡ This was a rice association with a larger purchasing than marketing business.

§ These two poultry coöperatives did a larger purchasing than marketing business.

sented below were received from a questionnaire sent to all California marketing and purchasing coöperatives (See Appendix A).

Of 228 California coöperatives replying to a questionnaire, 203 (89.0 per cent) used marketing contracts. Only 25 (11.0 per cent) did not (table 1). Of the coöperatives not using marketing contracts, seven were purchasing coöperatives. Three of the others (one rice and two poultry associations) might also properly be classified with purchasing coöperatives, since their supply business exceeded their marketing business. Two of the four dairy associations without contracts were bargaining associations. Thus, of the 25 coöperatives not using contracts in 1954, only 13 were primarily marketing associations, and one of these reported that it was going to begin using a contract in the near future. These 13 coöperatives not using contracts marketed livestock, fruits and vegetables, dairy products, and honey.

The two livestock marketing associations apparently do not use contracts because they are not very practical or necessary in this type of organization. Livestock producers may find it feasible and desirable to market through a number of alternative marketing channels depending on marketing conditions. Because their livestock associations are not represented in all markets, members cannot always sell through them. Moreover, it is not vital for efficient operation that every transaction be made through the livestock associations, because they do not have large capital investment to protect. Rather, these associations act primarily as agents or brokers for their patrons in central markets or local auctions.

Some fruit and vegetable marketing associations (excluding those handling citrus and grapes) do not use marketing contracts (table 1). This is true of eight such coöperatives in our sample. All of these were either small local or centralized associations doing an annual business of between $100,000 and $700,000. Because of their size or for other reasons, they either have never used marketing contracts or have abandoned them.

One of the two dairy marketing associations (in addition to the two bargaining associations mentioned above) not using marketing contracts is a small local coöperative. The other has annual sales exceeding $10 million and is the only large California marketing association not using a contract. Its members are bound to the association primarily by the confidence it has built up during its fifty years of successful operation.

Except for these few cases, all of California's marketing coöperatives in our sample use marketing contracts of one sort or another.

The figures given above include *all types* of associations—local, centralized, and federated associations. In the case of 11 central associations of federated coöperatives in our sample, all but one purchasing central have marketing contracts with their local associations. These include federated coöperatives in the following fields: one each in dairy, deciduous fruit, dried and canned fruit, vegetables, and nuts; and two each in citrus, purchasing, and wines.

These facts indicate that today about 90 per cent of California's coöperatives use contracts. If we exclude purchasing associations, about 92 per cent use contracts. Available evidence does not permit comparisons between present and past use of contracts by the coöperatives in our sample. We can, however, make an interesting comparison between the extent of this practice by present and past California coöperatives. Between 1875 and 1939 at least 430 California coöperatives (almost as many as are operating in the state today) went out of business, and 70.8 per cent of these used marketing contracts (Cochrane and Elsworth, 1943). This indicates that a greater percentage of California coöper-

atives use contracts today than did in the past. It is also interesting that in California there were more discontinuing coöperatives that used contracts than in any other state. New York was second with 54.3 per cent and Washington third with 52.1 per cent. The average for all states was only 27.6 per cent.

If we assume that our sample of each commodity group is representative, we can estimate how many California coöperatives use marketing contracts. We have made such estimates in table 1. According to these estimates, 423 (88.7 per cent) of the state's 477 coöperatives use marketing contracts. If we exclude purchasing coöperatives, about 92 per cent of the state's associations use contracts.

Forms of Marketing Contracts

Bylaw versus separate contracts. California coöperatives use many different types of contracts, but all contracts take one of two general legal forms. The oldest contract form spells out the marketing duties and rights of patrons in the association bylaws. This procedure usually includes all marketing obligations under a particular bylaw article. For example, citrus associations, most of which still use this form of contract, include most marketing provisions in a bylaw typically entitled "Marketing of Fruit." In some cases, the marketing provisions appear in several articles of the bylaws.

Through the years more and more coöperatives have included all the marketing duties and rights of patrons in a separate legal document variously called marketing contract, marketing agreement, membership agreement, agency agreement, crop agreement, or simply, agreement (see Appendixes A and B). When coöperatives use this form of contract, members must sign the marketing contract as well as the association bylaws.

There is no significant difference between the types of provision found in separate marketing contracts and those spelled out only in bylaws. For example, in citrus, where about two out of three local associations use only bylaws, practically all associations have identical marketing provisions (table 3).

Apparently the main reason coöperatives choose one contract form over the other is the matter of convenience and clarity. There is no significant legal difference. Including all marketing provisions in the bylaws has the advantage of greater simplicity: only one legal document is needed. On the other hand, separate contracts have the advantage of isolating all the marketing obligations of both parties and assembling them in a separate legal document where provisions can be spelled out in greater detail.

Most California associations apparently feel the latter advantage outweighs the former. Of the 117 coöperatives supplying us with their marketing contracts as requested, 76 used separate contracts and 41 included all their marketing provisions in their bylaws.

In this discussion, the term "marketing contract" refers to marketing obligations spelled out in either bylaws or separate marketing contracts.

Agency versus purchase-and-sale contracts. In addition to the differences in form of contracts mentioned above, there are also some important legal differences involving the legal ownership of a patron's product while the coöperative has possession of it.

California coöperatives use both "agency" and "purchase-and-sale" contracts. As a general rule, an association will use an agency type of contract when either or both of the following conditions obtains: (a) the separate identity of each member's product is to be maintained from time of delivery to time of sale, and (b) the period of time between delivery to the association and sale is relatively short—say not more than a week or two. On the other hand, an association generally uses a purchase-and-sale contract

if (a) the products delivered by individual members are to be pooled or commingled, and/or (b) a considerable time lapses between delivery and sale, as, for example, when products have to be processed or stored.

Agency contracts make the coöperative the legal agent of its members in marketing their crops. This permits the association to use its discretion in marketing such crops, but the patron keeps legal title to them. This means that the grower assumes any price or other risks to which his products are exposed while the association handles them. The following clause from a fig association's marketing contract is a typical agency contract clause:

> The grower hereby appoints the association the sole and exclusive agent of the grower for the sale and handling of the grower's fig crops, and also as attorney in fact of the grower for such purpose.

Under **purchase-and-sale contracts,** the association takes title to its members' crops as well as control over marketing them. The following clause from a walnut association's marketing contract is a typical purchase-and-sale contract clause:

> Local agrees to buy of and from Grower and Grower agrees to sell and deliver to Local all of the walnuts produced by Grower.

Each type of contract has certain advantages. Agency contracts sometimes favor the patron. If a coöperative becomes insolvent, creditors cannot satisfy their claims against it by seizing patrons' crops held by the association (Hulbert, 1942, p. 125). There is one important exception to this general rule, however. If a clause in an agency contract permits the association to borrow on a patron's product, creditors may seize the crop even though title has not passed to the association (Hulbert, 1942, p. 124).

Purchase-and-sale contracts may make an association's selling job easier. Some buyers may prefer to do business with an association if it actually has title to the things it sells. This makes it easier

Table 2. Number of Agency and Purchase-and-Sale Marketing Contracts Used by California Marketing Coöperatives, by Commodity Groups

Type of association	Number of coöperatives in state using contracts*	Number of coöperatives with agency contracts		Number of coöperatives with purchase-and-sale contracts	
		In sample	Estimated number in state †	In sample	Estimated number in state †
Citrus	173	25	131	8	42
Wine	28	0	0	9	28
Other fruits and vegetables	115	13	38	27	77
Field crops	38	5	21	5	17
Dairy	19	3	11	2	8
Poultry	17	2	9	2	8
Nuts	26	1	2	15	24
Total	416	49	212	68	204

* This estimate is taken from column 5 of table 1. Because we received no marketing contracts from purchasing or miscellaneous associations, they are not included in this table.

† This estimate is based on the assumption that the ratio of agency to purchase-and-sale contracts for each type of association is the same for the entire population as for the sample. See footnote to table 1.

for the buyer to find out if the title to the product is clear.

There is no difference between these two types of marketing contract so far as enforcement of performance is concerned. The California Agricultural Code gives coöperatives the same enforcement remedies in each case (see pp. 13–14).

Of the 117 contracts inspected, 49 (41.9 per cent) were agency contracts and 68 (58.1 per cent) were purchase-and-sale contracts (table 2). In some fields one type is much more common than the other. In citrus, for example, about three out of four associations use agency contracts. In other fruits, in vegetables, and in nuts, the bulk of the associations use purchase-and-sale contracts. In other fields there seems to be no significant preference for one type over the other.

Again, if we generalize the findings of our sample to all California coöperatives, we can estimate that slightly over half the California associations use agency contracts (table 2).

Duration of Marketing Contracts

Local and centralized coöperatives. Of the 192 local and centralized coöperatives in our sample using marketing contracts, 154 (80.2 per cent) have contracts that are, in effect, only of one-year duration. Fifteen use straight one-year contracts. Another 104 use so-called "continuous" or self-renewing contracts. All but one of the continuous contracts in table 3 remain in force until the member notifies the association of his intention to withdraw. Such "continuous" contracts always specify a given period (varying from a few days to several months) of each year during which patrons may withdraw from their association. One continuous contract runs until the member sells his stock in his association to another party who then assumes the contract's obligations. Another 35

Table 3. Length of Marketing Contracts of Centralized Coöperatives and Locals of Federated Coöperatives in California

Length of contract	Number of coöperatives using contracts		Number of coöperatives with annual withdrawal privileges		Number of coöperatives with annual withdrawal privileges after initial contract period		Number of coöperatives without annual withdrawal privileges	
	Number in sample	Estimated no. in state*	Number in sample	Estimated no. in state	Number in sample	Estimated no. in state	Number in sample	Estimated no. in state
"Continuous"	104	245	104	245	0	0	0	0
1 year	15	38	15	38	0	0	0	0
2 years	23†	38	1	2	16	26	6‡	10
3 years	2	4	0	0	1	2	1	2
5 years	13	29	3	7	1	2	9	20
7 years	4	9	0	0	0	0	4	9
10 years	2	5	2	5	0	0	0	0
15 years	29	43	29	43	0	0	0	0
Total	192	411	154	340	18	30	20	41

* These estimates were made in the same way as those in table 1. See footnote to table 1 for an explanation of method used to apply sample to state figures.

† Includes three "continuous" contracts that provide for withdrawal annually, withdrawal becoming effective a year after notice has been given; they are therefore actually 2-year contracts.

‡ Includes one coöperative with a 15-year contract with withdrawal permitted every two years.

contracts, varying between 2 and 15 years, include annual withdrawal privileges similar to those specified in "continuous" contracts. Three "continuous" contracts in our sample provide for withdrawal annually, but withdrawal does not become effective until a year after notice has been given. They are, therefore, actually two-year contracts and have been counted as such in this study.

Eighteen (9.4 per cent) other contracts permit annual withdrawal after an initial period of membership beyond one year. For example, 16 contracts provide that after two years of membership a member may withdraw annually. One contract permits annual withdrawal after two years of delivery, and another after five years.

Only 20 (10.4 per cent) of the contracts in our sample have continuing nonwithdrawal contracts exceeding one year. Nine have five-year and four have seven-year contracts. One of these five-year contracts permits withdrawal after two years on the condition that members give the association, as "liquidated compensation," their accumulations in the association's reserves.

Assuming our sample of each commodity group to be representative of the entire group, we made the following estimates (table 3): 340 (82.7 per cent) California coöperatives use one-year contracts. Thirty (7.3 per cent) use contracts that have annual withdrawal privileges after an initial period of membership of between two and five years. Only 41 (10.0 per cent) use contracts exceeding one year which do not have annual withdrawal privileges, either annually or after an initial period of membership.

Federated coöperatives. Apparently, the "central" associations of federated coöperatives do not have significantly different contract periods with their "locals" than do the locals and centralized coöperatives listed in table 3. None of the 11 "centrals" using contracts use continuing contracts exceeding one year.

Four "centrals" have contracts with their locals permitting annual withdrawal after an initial contract period. The central of a supply association has a five-year contract that permits annual withdrawal thereafter. California's largest dairy central has a "ten-year" contract, but it permits annual withdrawal after three years of membership. A wine central has a contract with its locals permitting annual withdrawal after three years. A dried fruit central permits its locals to withdraw annually after two years. Locals are permitted to withdraw annually from six other marketing centrals (two citrus, one vegetable, one deciduous fruit, one nut, and one wine). Finally, the central of a federated purchasing coöperative does not have any contract with its locals.

Why Are Short-term Contracts Used?

These facts indicate that the great bulk of California coöperatives do not depend upon marketing contracts to maintain membership loyalty for periods exceeding one year. Even most of those associations with contracts exceeding one year permit annual withdrawal after two to five years of membership. This situation apparently represents a significant change over the types of marketing contracts commonly used in the United States during the 1920's. A 1924 study revealed that 55 (58.5 per cent) of the 94 American coöperatives studied (all of which used contracts) had nonwithdrawal contracts of three to seven years' duration (Johnson, 1924, p. 2). Forty of these were five-year nonwithdrawal contracts.

What factors are responsible for this general acceptance of one-year marketing contracts by California coöperatives? Familiarity with California experience suggests the following hypotheses.

First, many associations have found

that some members resent long-term contracts. Thus, benefits from long-term contracts are more than offset by the barriers to membership resulting from them.

Second, most California coöperatives are so well established today that they need not depend on long-term contracts to give them an opportunity to prove themselves.

Third, annual contracts adequately protect associations against most potential causes of patron nonperformance.

Fourth, California coöperatives have other ties with their patrons, which make it unnecessary to bind them with marketing contracts for long periods.

Let us see what evidence there is to support these hypotheses.

Do long-term contracts deter membership? Available evidence suggests that marketing contracts discourage some patrons from doing business with coöperatives. In answer to the question on this point, 153 California coöperatives having marketing contracts expressed an opinion. Twenty-five, or about one out of six, felt that contracts did tend to deter producers from joining an association.[7] This is significant in view of the fact that the great bulk of the associations in our sample used only one-year contracts. As one might expect, a higher proportion of the coöperatives with contracts exceeding one year stated that their contracts deterred membership. Of the 17 coöperatives with nonwithdrawal contracts exceeding one year which responded to the question, ten indicated that their marketing contracts do tend to deter some farmers from joining. Moreover, those coöperatives not using contracts often gave as their reason for not doing so the belief that such contracts deter membership. These facts support the hypotheses that marketing contracts of even one year may deter some potential members from joining coöperatives, and that contracts of longer duration deter a greater number.

Of course this tells only part of the story, representing the point of view of management rather than members. Doubtless many patrons would not be willing to join an association if they were not assured of contracts. Therefore, the net effect of contracts very likely is to increase coöperative membership. But this evidence does indicate that patron resentment to long contracts is one important reason why more California coöperatives do not use longer-term contracts. Moreover, our conversations with coöperative leaders also support this conclusion.

How well established are today's coöperatives? Another possible reason for the short-term contracts is that most California coöperatives have long, successful histories. Therefore, they are less dependent on long-term contracts than are newly founded associations. In 1923 California's Aaron Sapiro, a strong advocate of long-term contracts, expressed their need in the case of new associations as follows (Bakken and Schaars, 1937, p. 323n):

> The contract should always be a long-term agreement. It is impossible for farmers in a period of less than three years to develop a trained personnel, to perfect the process of receiving the commodity, to make good and wise commercial connections and to effect satisfactory banking arrangements. The rule is rather sound; a short-term contract is hardly worth the paper it is written on. A long-term contract gives the farmer a chance. There should be no right of withdrawal whatsoever, except at the end of a specified long term. If the farmers intend to try the coöperative marketing system, they should go into that work seriously, earnestly, and on a permanent basis.

This argument for long-term contracts is strongest for newly organized coöpera-

[7] A better indication of membership attitude toward contracts could be obtained from members rather than management. Perhaps a still better indication could be derived from asking nonmembers of associations with long contracts whether the contract period acts as a deterrent to joining the association. Neither of these approaches was undertaken in this study.

tives. Therefore it does not apply in the case of most California coöperatives today. Of the 207 marketing associations giving us this information, 77 (37.2 per cent) were formed before 1920, 126 (60.0 per cent) before 1930, 178 (85.9 per cent) before 1940, and 186 (89.9 per cent) before 1945. This indicates that nine out of ten of California's marketing coöperatives in our sample have been in business for ten or more years.

Because most of California's coöperatives had long ago proved that they were efficient organizations, the need for long-term contracts to "get their organizations started" no longer exists. That California coöperative sentiment still favors longer contracts for new associations is supported by the nature of the contracts of marketing associations formed since 1940. Of 27 marketing associations formed since 1940 which use contracts, 14 have contracts exceeding one year. Three of these have seven-year nonwithdrawal contracts; seven have five-year nonwithdrawal contracts; one has a straight two-year contract; one has a five-year contract with an annual withdrawal privilege after five years of membership; and two have contracts permitting annual withdrawal after two years of membership. These relatively new associations apparently feel that they need longer contracts to get their associations under way.

Do annual contracts meet nonperformance problems? Another factor tending to encourage the use of one-year contracts may be that such contracts give ample protection against most forms of nonperformance. Empirical evidence to test this hypothesis is hard to come by. But we can make some meaningful observations by analyzing the types of situation responsible for nonperformance.

The prospect of getting higher net prices by selling outside of their association is chiefly responsible for patron nonperformance. This opportunity may develop for several reasons. It may arise if a coöperative attempts to raise prices for its members through market control. To raise market prices significantly, a coöperative must do two things: (1) it must have most of the producers as patrons; and (2) in the absence of production controls, it must divert part of the supply from regular market channels—either by exporting, dumping, or processing or diverting it to some lower price use. The immediate effect of such actions is to raise prices in the primary markets above competitive levels. This may give coöperative patrons a blended price—a weighted average of the price of the product sold in the primary and secondary market—which is higher than they would otherwise have received. But this is only part of the story. Noncoöperative members may be benefited even more than members by such a program. Because they are able to sell all of their output in primary markets, nonpatrons receive net prices exceeding the blend prices of members. Coöperative members, seeing this, have a powerful incentive to desert their association in subsequent years. Consequently, associations having price enhancement or stabilization as a primary objective must have contracts exceeding one year.

But experience has demonstrated that even long-term marketing contracts are not enough to permit coöperatives to achieve significant monopoly power. As more and more members leave the association, and as production is expanded (both by members and nonmembers) in response to the noncompetitive price levels, the burden of the diversion program becomes excessive. The blend prices of coöperative members fall so far below nonmember prices that mass desertions of members occur until the association either goes out of business or changes its objectives.[8]

[8] The experience of the South Carolina Cotton Growers provides an interesting example

During the 1920's some California coöperatives attempted to imitate the monopolistic behavior of nonagricultural concerns, but none of these associations succeeded for long. Since then the associations have changed their objectives primarily to increasing patrons' returns through more efficient marketing. Although many coöperatives still take an active interest in price enhancement and stabilization, they have generally not tried to accomplish this through their own activities. Instead, federal or state marketing-order programs are used to this end. These programs treat all growers in the industry alike; therefore, marketing through coöperatives in the industry involved is neither encouraged nor discouraged. They may indirectly reduce coöperative membership, however. Growers are usually most conscious of marketing savings in times of low prices. Therefore, insofar as state or federal marketing-agreement programs enhance prices, growers may have less incentive to join coöperatives. But the net effect of this incentive is likely to be very small.

Because today's California coöperatives do not have monopoly pricing as an objective, the price incentive does not tempt members to leave the association as it inevitably would otherwise. Therefore this reason for long-term marketing contracts no longer exists.

California coöperatives today are not confronted by the above-mentioned causes for member disloyalty, but other causes still exist. The incentive for temporary patron disloyalty may become especially strong in times of abnormally short supply or high demand. When supply is abnormally short, noncoöperative marketing organizations may make every effort to attract some coöperative patron business so as to operate nearer capacity. As long as all marketing agencies, including coöperatives, pay the same price to all comers, coöperative members have no price incentive to sell outside their association. But some noncoöperative marketing concerns may offer slightly more than the market price to get certain growers' business. Coöperatives are unable to cope with such "competition" because they must pay all growers identical prices, particularly when they sell on a pool basis. Therefore some patrons have a price incentive in such cases to sell outside their association. For this to occur, however, price competition must be limited. It is most likely to happen in industries where coöperatives have only a few rivals. Such market structures are common in many agricultural processing industries. In such oligopolistic markets (markets of few buyers) competition generally does not force buyers to pay identical prices to all sellers. This permits the above-mentioned type of price discrimination between growers to occur, with its consequent undermining of patron loyalty.

One-year marketing contracts are as effective in preventing such nonperformance as are longer contracts. Growers generally are unable to know at the time of signing their annual contracts whether or not supply is going to be abnormally short. Even if the grower anticipated a short supply, he might not be sure that he would be singled out by competitors for special price treatment. Consequently, he would probably decide to sign a contract with his coöperative if past experience proved that it usually paid growers average market prices or better. Thus, this type of threat to member loyalty can usually be met as well by annual contracts as by longer-term ones.

---

of this process. In 1922 it signed up 11,434 cotton growers. Before their five-year contract expired in 1926, 71 per cent of the members refused to sell through the association. After the contract expired in 1927, all but 8 per cent had left the association. Obviously by this time, it had lost whatever monopoly power it had in the initial years. (Wilson Gee and Edward A. Terry, *The Cotton Cooperatives in the Southeast* (New York: D. Appleton-Century Co., 1933), p. 160.

Short-run price changes may also encourage a patron to sell all or part of his crop outside his association. This situation arises whenever coöperatives pool members' crops. For example, suppose an egg-marketing association is using a two-week marketing pool. Under such an arrangement, all growers delivering eggs of a certain quality during a two-week period receive the average market price for such eggs. Should market prices suddenly rise near the end of a pooling period, a grower belonging to this association would have an incentive to sell outside it, for the price he could expect in the open market would be higher than the average pool price he would get from his coöperative. Such opportunities would be most likely to arise when prices fluctuate greatly and when the pooling period is long. Seasonal price variations fluctuate widely for most agricultural products, and many coöperatives use quite long pool periods. For example, the local citrus associations belonging to Sunkist Growers, Inc., use pooling arrangements varying from two weeks to an entire season (Gardner and McKay, 1950, p. 36).

For coöperatives to operate most effectively under such conditions, they must have a legal tie to insure delivery. One citrus coöperative official commented, "When prices fluctuate sharply in response to both market and supply, . . . I am sure the existence of our membership contracts is the only thing which insures our fruit supply."

This threat to delivery makes marketing contracts essential. But again, one-year contracts are as effective as longer ones in preventing nondelivery due to this problem. This is true because during the annual period when patrons can withdraw from their association, they are unable to predict whether they are going to benefit or lose by selling on a pool basis in the future. Actually, they may usually prefer the prospect of getting at least the season average price rather than take the chance of more or less. Therefore they may be willing to sign a marketing contract binding them against nonperformance. Once having signed the contract, they are again bound for the entire season. So long as the patrons remain convinced that the pool is being run judiciously—accurately reflecting quality differences, etc.—they do not withdraw from their association.

Noncontractual considerations encouraging coöperative membership. A final reason why coöperatives may not need longer marketing contracts is that certain nonlegal considerations encourage continued participation in coöperatives. These may be social, political, or economic. Patrons may prefer coöperation as a "way of economic activity." They may believe that by belonging to a large, politically articulate coöperative, they may be able to enhance their long-run social, political, and economic interests. These and other noneconomic considerations may serve as strong bonds between coöperatives and their patrons. But here we shall consider only some of the chief economic considerations encouraging continued patron participation.

Perhaps the strongest nonlegal tie between patrons and their coöperative is the patrons' belief that their coöperative is doing a good job. If patrons feel that their coöperative on the average pays equal or higher returns than other businesses, they will not readily be tempted to sell elsewhere. They know that should they sell elsewhere, they may be expelled from the coöperative and not be permitted to sell through it in the future. Even if they wait until their marketing contract expires, they may not be able to rejoin their coöperative in the future (see page 47.)Thus, patrons who would gain a temporary advantage by leaving their coöperative may remain in it even when not legally bound to do so. They realize that it is against their long-run

economic interest to do otherwise. Of course, if expelled or withdrawing patrons could rejoin an association at their discretion rather than at the coöperative's, probably many would leave to sell on the outside whenever it was profitable to do so. So the above economic incentive for remaining within a coöperative is made more effective by the coöperative's right to refuse membership to expelled and other past members.

Every coöperative ultimately must engender this feeling of economic adequacy in the minds of its patrons. Without it a coöperative cannot hope to survive, much less grow. And while marketing contracts may contribute to a coöperative's efficiency, they are but one of the many factors in determining its ultimate success.

Another economic bond tying patrons to their coöperative may be created by the revolving-fund method of financing, which is widely used by California cooperatives. This bond, which is not a legal one, may be created under the following circumstances.

The price and patronage rebates cooperatives pay patrons may represent not only a payment for the patron's commodity, but may also include a payment or return on his investment in his coöperative. This is not necessarily true if the coöperative pays interest on its invested capital. But because many California coöperatives do not pay interest on their revolving-fund certificates, patrons, in effect, do get a return on invested capital included in their patronage payments from their coöperative. Such payment may be more or less than a patron's proportionate investment in his coöperative. This comes about primarily because whereas the annual deductions for revolving funds customarily are proportional to patronage, new members do not have as much in the revolving fund. For example, during his first year of membership, a patron receives the use of the coöperative's capital facilities although he has made practically no investment in the association. But generally, the revolving-fund method of financing tends to make a patron's investment in his coöperative proportional to his patronage.

Informed coöperative patrons are aware of this fact and take it into consideration when estimating how the returns received from their association compare with prices paid by other marketing institutions. A patron has an economic incentive to quit his coöperative whenever prices paid elsewhere exceed those paid by his coöperative, less that part of the coöperatives' prices representing a return on his investment. But should he be unable to withdraw immediately his entire investment from his coöperative, his decision might well be different. For example, suppose he was selling through a coöperative financed entirely by a seven-year revolving fund. Then his investment in his coöperative might be considerable, especially if it owned processing facilities. Should he leave his association, he would receive no interest on his investment and would be repaid his principal at the rate of one-seventh each year. Coöperative bylaws or marketing contracts invariably provide that members quitting an association be repaid their equity in revolving funds at the same time as if they had remained in the association (see page 47).

Thus, for seven years, in the example given above, the patron would have to forego any earnings on all or part of his investment in the association's revolving fund. (This is not to say that he is treated unfairly, for when he joined the association he, in effect, received a return on someone else's investment until he had been in the association for some time.) Such a possibility may act as a powerful deterrent to a member considering leaving an association. The relative importance of this form of economic bond between a coöperative and its patrons will vary with the size of the revolving fund

and its period of revolution. For example, in wine coöperatives the average period of revolution is about nine years. The average investment of patrons who have been in these associations for nine years exceeds $10,000. A member with an investment of $10,000 in a nine-year revolving fund would be faced with this prospect: If he left his association, he would be repaid $1,100 of his principal each year for nine years. If he remained in it, he would receive the market price for his products sold through it, plus a premium representing a return on his investment in it. If his coöperative earned 10 per cent on his investment, this return would amount to $1,000. This would be about the same as the principal he would be repaid each year upon leaving the association. This could prove a strong incentive for him to remain in the association.

This deterrent to withdrawal may be especially strong between locals of federated coöperatives and the centrals of such associations. The legal bond between locals and centrals is usually short, but the economic bond created by the locals' interest in their central's revolving fund may be very great. All of California's large federated coöperatives are financed by revolving funds. The individual local's share in the central's revolving fund may run into hundreds of thousands of dollars (one local wine coöperative has nearly $1,000,000 invested in its central's revolving fund), and the funds may revolve in a 10-year cycle. Under these circumstances, a local association would be very hesitant about striking out on a marketing venture of its own.

Insofar as the conditions assumed above apply to specific coöperatives, the revolving-fund financing method may serve as a strong economic bond between members and their associations. And since most California coöperatives do use revolving funds, they may often strongly supplement the legal bond created by marketing contracts.

Summary. All four of the reasons discussed above apparently encourage or permit coöperatives to use short-term contracts. Doubtless the relative importance of these reasons varies during an association's development, and some reasons may seldom or never apply to coöperatives handling certain commodities.

Some coöperatives may have sound economic reasons for using long-term contracts; others may not. Some may continue to use long-term contracts after the need for them disappears. They may reason that as long as patrons do not strongly resent long contracts, there is no need to shorten them. They may be right. But such associations should ask themselves these questions: Have conditions changed significantly since we fixed the initial contract period of our marketing contracts? If so, can and should we reduce our contract period?

The ultimate answer to these questions rests with the peculiarities of each association. But the fact that nearly all well-established associations find short-term contracts adequate suggests that long-term contracts are not necessary for efficient operation, except perhaps for the first two to five years of an association's life. Thus, all associations using long-term contracts should periodically ask and answer these questions.

Enforcement Provisions

Types of provisions. Marketing contracts set forth the ways in which farmers agree to become integrated with their coöperatives. When farmers agree to a contract they almost invariably intend to keep their part of the bargain—and they nearly always do. But experience has clearly shown that circumstances often arise which make it appear advantageous for some farmers not to live up to their part of the bargain. Then the value of the contract as a legally enforceable document becomes important. Contracts take on new meaning because the courts recognize them as bona fide legal agree-

ments giving the injured party certain legal remedies. Without this promise of assistance from the courts, marketing contracts would be mere pieces of paper setting forth the moral promises of each party to do certain things.

The California Agricultural Code permits coöperatives to use three types of legal remedy to enforce their market contracts: liquidated damages, specific performance, and injunction. Nearly all California marketing contracts include specific provisions permitting the association to use one or all of these remedies to insure patron performance. Of the 117 such contracts inspected, all but three (marketing cotton, deciduous fruit, and rice) included provisions for liquidated damages, and 45 also included provisions for injunction and specific performance.

No contracts provided for injunctions and specific performance without also providing for liquidated damages. Some coöperatives including provisions for all types of remedy also included a provision giving them the right to select the most appropriate one. For example, one association has the following provision:

> No remedy herein conferred upon Association is intended to be exclusive of any other remedy, but each and every such remedy shall be cumulative and shall be in addition to every other remedy given herein or now or hereafter existing in law or equity or by statute. Association may enforce any or all of such remedies either separately or concurrently.

Methods of setting damage. All contracts providing for liquidated damages spell out the extent of such damages. California associations set damages in four different ways.

Absolute amounts. Most typically, these provisions set a *specific absolute amount* to be paid as liquidated damages for each unit of a commodity sold outside of the association. For example, most citrus contracts fix damages at $0.25 a box. A typical provision setting damages of a fixed absolute amount reads:

> The parties hereto fully understanding and admitting that it will be impractical or extremely difficult to fix the actual damages to the buyer which will result from the breach of this contract by the seller hereby expressly agree and stipulate that in the event of the seller's neglect, failure or refusal to deliver to the buyer the fruit purchased hereunder, the seller will pay the buyer the sum of $0.25 per box for all fruit covered hereby, and undelivered as liquidated damages for such breach.

Of the 117 contracts inspected, 96 (82.0 per cent) fix damages at some absolute amount.

Per cent of market value. Eleven prune and apricot marketing associations and one wine association in our sample fix damages at 20 per cent of their market value. One dairy association also fixes damages in this way, setting damages at 15 per cent of the product's value.

Equal to share of fixed cost. The third most frequent method of setting damages is to fix them equal to the nonperforming member's share of the association's fixed cost. One wine and six prune-dryer associations in our sample set damages this way. The prune-dryer associations' contracts permit them to assess damages

> equal to the proportionate cost, as determined by the Dryer, of the upkeep and maintenance of the dryer and drying equipment, including overhead of the Dryer (except labor, fuel and power actually expended by the Dryer in the dehydration of the prunes of the members of the Dryer) based on the number of tons of fresh prunes agreed to be delivered by him.

The wine association fixing damages in this way directed the Board of Directors to

> levy an assessment against such stockholders to cover his proportion and share of the fixed charges for each year separately during which the said stockholder refuses to deliver . . . his entire allotment of grapes.

Equal-to-marketing charge. A deciduous fruit association uses a fourth method of setting damages. It fixes damages equal to the marketing charge it would have received had it marketed its patrons' products. This association fixes

such marketing charges each crop year.

Minimum damages. Another fairly common feature of liquidated damages provisions is to fix a minimum amount of damages as well as a specific amount per unit. For example, a citrus coöperative has a provision for damages of $0.25 per box with minimum damages of $25 per violation. An avocado association fixes minimum damages at $1,000 plus $0.05 a pound for all avocados not marketed through it. In all, 17 of the contracts inspected included similar minimum damage provisions.

Relative size of damage provisions. The relative size of liquidated damages set by California coöperatives varies greatly. Table 4 compares the liquidated damages for various commodities with their market value in 1953 and 1939. (This comparison includes

Table 4. Extent of Liquidated Damages for Various Products Marketed by California Coöperatives and Comparison at 1953 and 1939 Prices

Product	Number of contracts	Extent of damages		Liquidated damages as per cent of average prices received by California farmers	
		Dollars	unit	1953	1939
Cotton	4	$ 1.00	Bale	0.6	2.1
Flaxseed	1	0.25	Bushel	6.6	15.6
Butter	1	0.05	Pound	7.7	18.1
Honey	1	0.01	Pound	7.9	18.9
Dairy products	5	*0.05** 15% of value	Pound	*3.6–15*	*10*–15
Eggs	2	0.05	Dozen	9.4	23.1
Apples	2	8.00–10.00	Ton	9.5–11.9	38.1–47.6
Strawberries	2	0.50–1.00	Crate	7.2–14.4	18.1–36.2
Pears	5	6.00–*10.00*	Ton	8.3–13.8	19.5–*39.0*
Peaches	5	6.00–10.00	Ton	9.9–16.4	28.6–47.6
Lemons	17	*0.25*–.75	Box	7.2–21.6	*16.7*–50.1
Walnuts	14	0.03	Pound	14.6	34.7
Grapes (Wine)	8	*5.00*—20% of value	Ton	*11.6*–20	20–*36.5*
Beans (Kidney)	1	2.00	Bag	16.8	37.3
Cottonseed	1	10.00	Ton	18.8	36.5
Olives	4	10.00–60.00	Ton	5.6–33.6	13.2–79.2
Apricots and prunes	11	20% of value	......	20	20
Hay	2	3.00–5.00	Ton	14.3–23.8	33.7–56.2
Oranges	25	*0.25*–.50	Box	*15.2*–30.4	*20.2*–41.0
Almonds	1	0.05	Pound	21.2	47.6
Chickens	1	0.25	Bird	24.5	48.1
Avocados	1	0.05	Pound	27.0	65.8
Beans (Lima)	3	0.02	Pound	17.2	42.0
Raisins	1	0.03	Pound	35.9	124.0
Figs	1	0.03	Pound	40.0	76.9
Total†	119				

* Italicized figures represent the most frequently used liquidated damage provision found in the marketing contracts of a particular commodity.

† The number of cases listed here and in table 5 differs from the number of contracts (109) which set damages of a fixed amount or percentage. This difference arises because some associations marketing several products (e.g., citrus) use the same contract for each.

only the 109 associations setting damages at some absolute amount or at some percentage of the product's market value.) This comparison indicates that in 1953, liquidated damages ranged from 0.6 per cent of the farm value of cotton to 40 per cent in the case of figs.

Table 5 summarizes the material presented in table 4. It shows that at 1953 prices, 112 (94.1 per cent) contracts in our sample fix damages at under 30 per cent of the products' market value. At 1939 prices, only 64 (53.8 per cent) would set damages at under 30 per cent.

The extent of damages varies not only among commodities but also among coöperatives marketing the same commodity. In olives, one coöperative sets damages at $10 a ton, whereas another fixes damages at $60 a ton. These damages represented 5.6 and 33.6 per cent, respectively, of average olive prices in 1953. In lemons, the assessable damages vary between $0.25 and $0.75 a box, and in oranges, between $0.25 and $0.50 a box. But for the most part, coöperatives in a particular industry set identical damages. In cotton, all four contracts inspected set damages at $1.00 a bale. In lemons and oranges, the great bulk of the associations fix damages at $0.25 a box. In deciduous fruits, the most frequent amount is $10.00 a ton. In some federated coöperatives, all local associations have identical liquidated damages provisions. This is true of walnut locals. But in citrus the locals of the country's largest association, Sunkist, use a variety of liquidated damages provisions.

Because many agricultural prices fluctuate greatly, the relative costs of damages to nonperforming farmers vary when contracts set damages of a fixed absolute amount. For example, in 1953, the $1.00-a-bale damage provision represented only 0.6 per cent of the market value of cotton (table 4). But at 1939 prices, it represented 2.1 per cent. Similarly, liquidated damages in figs represented 40 per cent of market value in 1953 contrasted to 76.9 per cent in 1939.

Table 5. Estimated Number of California Marketing Contracts Having Liquidated Damage Provisions of Various Sizes: A Comparison with 1953 and 1939 Farm Prices

Liquidated damages as a per cent of the price of the product	1953 farm prices of relevant products		1939 farm prices of relevant products	
	No. of contracts in sample	Cumulative per cent of total	No. of contracts in sample	Cumulative per cent of total
0– 9.9	21	17.6	4	3.4
10–19.9	70	76.5	23	22.7
20–29.9	21	94.1	37	53.8
30–39.9	6	99.2	33	81.5
40–49.9	1	100.0	13	92.4
50–59.9	0	.....	4	96.1
60–69.9	0	.....	1	96.9
70–79.9	0	.....	3	99.3
80–89.9	0	.....	0	.....
90–	0	.....	1	100.0
Total	119	100.0	119	100.0

With damages of fixed amounts, the relative burden of nonperformance varies as prices vary. Therefore, patrons are least likely to sell outside their association in times of relatively low prices. When damages are set at a fixed percentage of the market value, the situation is different. Then the relative burden of nonperformance remains unchanged as prices change.

The preceding facts demonstrate a considerable range in the relative size of liquidated damage provisions. There is variation both within commodity groups as well as among various groups.

Why do damages vary? Most variation within commodity groups can be explained only by the preferences of the individual associations. For example, there is little basis for believing that the damage suffered by one citrus packing house due to nonperformance is likely to be three times as great as for others. Yet although most associations fix damages at $0.25 a box, others set them at $0.35, $0.50, and even $0.75 a box. There seems to be no significant correlation between extent of damages provisions and (1) size of association, (2) average member volume, or (3) age of association. Each of these variables was checked in the case of local citrus associations, where damages provisions ranged from $0.25 to $0.75 a box.

But what of the differences from one commodity group to another? They may be explained in part by differences in the actual damages likely to result from nonperformance. Coöperatives performing the smallest marketing job are likely to be least harmed by a given amount of nonperformance. For example, the cost of ginning a dollar's worth of cotton is less than the cost of handling, processing, storing, and distributing a dollar's worth of raisins. We would expect damages provisions to reflect such differences. But while such differences may account for some variation between commodities, they do not account for all of the difference. For example, the costs of processing and marketing wine are much greater per dollar of sales than are hay-marketing costs. Yet the liquidated damages provisions are twice as great in hay as in wine. Inspection of table 4 will suggest other, similar anomalies.

The most significant measure of actual damages is not total marketing costs per unit but fixed costs per unit. If all costs are marginal costs, nonperformance by some members is not likely to raise the marketing costs of others very much. But usually associations with the highest total marketing costs per unit are also those with the highest fixed costs.

The preceding discussion supports the conclusion that much of the variation in liquidated damages provisions is not explainable primarily by differences in marketing costs. Other factors, which cannot be generalized, are responsible for these differences. Beyond the question of what practices do exist, there is the more important question of what practices should exist? How large should liquidated damages be? This question needs to be answered in both legal and economic terms.

How large should damages be?

Legal consideration. As pointed out earlier, most state statutes, as well as the common law, permit coöperatives to use liquidated damages as a remedy for nonperformance. But such legal sanction does not insure that the provision for liquidated damages in every coöperative marketing contract is legal merely because both parties have agreed to it. Legality is conditioned upon reasonableness. If the stipulated damages are wholly disproportionate to the actual damages, the courts may declare them "penalties" and therefore illegal (Packel, 1947, p. 155). This possibility may arise even if damage provisions are not disproportionate when initially made. For example, at 1953 prices, failure to deliver raisins could have resulted in liquidated

damages of 36 per cent of their market price (table 4). But should raisin prices return to 1939 levels, liquidated damages actually would exceed their market value by 24 per cent. The courts almost certainly would consider this a wholly disproportionate remedy and therefore a "penalty."

The precise legal dividing line between penalties and legal damages is not clear. A California court permitted damages of $0.05 per dozen of eggs at a time when this represented about 20 per cent of their market value.[9] Another California court sanctioned damages of $0.50 per hundredweight of milk at a time when this was 25 per cent of its value.[10]

Furthermore, the courts have not always agreed on the dividing line between liquidated damages and penalties. In 1926 a South Carolina court held damages of 5 cents per pound of cotton excessive. In the same year, an Oklahoma court ruled that damages of 5 cents per hundredweight of cotton were not unreasonable.[11]

Thus, it is impossible to predict what the courts will rule an excessive damages provision. But because courts are guided by the principle of "reasonableness," we can draw certain conclusions.

First, damages equal to a member's share of his association's fixed costs are never likely to be declared illegal, for they closely approximate the association's actual damages.

Second, in California, damages provisions for a specified percentage of the market value of a commodity are not likely to run into legal difficulties if they are about 20 per cent or less.[12]

Third, flexible damages provisions, fixing damages equal to the amount which would have been paid as a marketing charge, are also likely to be held reasonable by the courts. Here, the liquidated damages are likely to approximate closely the actual damages suffered.

Fourth, liquidated damages provisions providing for fixed absolute amounts may not be enforceable when this amount becomes wholly disproportionate because of falling prices.

Thus, purely on legal grounds, the first three methods seem preferable. But the shortcomings of provisions of the last-mentioned type can be overcome if they are adjusted as price levels change significantly.

Economic considerations. But what about the economic desirability of the various methods and levels of damages? Economically, liquidated damages provisions have two important functions: (1) to discourage patron nonperformance, and (2) to compensate the association for diseconomies caused by the withdrawal of patronage by some members. Very high damages provisions achieve both of these objectives. In fact, the higher the damages, the more completely will these functions be performed. But to assure equity for both performing and nonperforming patrons, the liquidated damages should approximate the damages resulting from nonperformance.

Ideally, damages should equal the decrease in net revenue suffered by performing members. In practice, however, it is impossible to set the exact amount of damages resulting from nonperformance before an actual breach occurs. This ideal measure can be approached, how-

[9] Poultry Producers of Central California v. Nilsson, 197, Cal. 245, 239 Pac. 1086.

[10] Milk Producers Assn. v. Webb, 97 Cal. App. 650, 275 Pac. 1001.

[11] South Carolina Cotton Growers v. English, 135 S.C. 19, 133 S.E. 542. Oklahoma Cotton Growers Assn. v. Salyer, 114 Okla. 77, 243 Pac. 232.

[12] The Wisconsin Coöperative Marketing Statutes provide that coöperatives may fix damages at "an amount equal to a certain percentage, not exceeding 30 per cent, of the value of products which are the subject of breach." But in one case the Wisconsin Supreme Court held that a contract providing for damages up to 20 per cent was illegal because it did not specify a *fixed* percentage. John Hanna, *The Law of Coöperative Marketing Associations* (New York: Ronald Press Co., 1931), p. 227.

ever, by setting damages equal to that part of an association's fixed costs which it would have charged against the nonperforming patron, for performing patrons are harmed primarily because overhead costs must be spread over a smaller business volume.

This is the correct measure of damages if three important assumptions are met: (1) that the association is selling in a perfectly competitive market; (2) that its marginal costs are constant over the relevant range; and (3) that the nonperformance of some members does not prevent an association from meeting its own contract obligations to third parties.

(1) When an association sells in an imperfectly competitive market, its members' returns depend not only on its costs per unit but its revenue per unit. Then the latter as well as the former will vary at different outputs. Consequently the appropriate measure of damages is the decrease in net revenue that performing members suffer because of some member's nonperformance. Under these conditions, actual damages might be greater or less than the nonperforming patron's share of fixed costs. It will depend on whether the association is operating short of, or beyond, its optimum output. Because it is extremely difficult to determine these facts in practice, fixing damages equal to a patron's share of fixed costs is likely to provide a good approximation of actual damages. This is especially true when the association's demand curve is quite elastic.

(2) But what about our assumption of constant marginal costs? Empirical evidence suggests that it is valid over quite wide ranges of output for many marketing establishments.

(3) When this assumption is not met, it is impossible to determine accurately the amount of damages suffered by nonperformance; they are even more hazardous to estimate well before a breach occurs. Because of this, liquidated damages is an inadequate form of relief. Other types of relief are then needed (see page 14).

Let us see how this ideal measure can be used in practice. In 1953 one California coöperative cotton gin estimated its total average cost at about $10.00 a bale. Its average fixed costs came to about $7.00 a bale. Suppose one of its patrons failed to deliver 100 bales he has pledged. Then, the $700 of overhead costs which otherwise would have been charged against him would have to be spread over performing members, and their costs would have increased by a corresponding amount. Consequently, he has damaged them to the extent of $700. He should therefore pay liquidated damages of $7.00 a bale, or $700. (This is actually $6.00 more per bale than cotton gin contracts require, table 4).

As pointed out above, seven associations in our sample set damages in this way. But how well do the methods most commonly used achieve this ideal?

Interestingly, the other legally most acceptable types of damages provisions may be least satisfactory economically. The *fixed per cent* of market value provision may well result in the most disproportionate type of damages. For example, suppose that when an association adopts its marketing contract, fixed costs per unit are about equal to 20 per cent of its product's market value. Then, if market prices should fall 50 per cent a few years later, such a damages provision would be inadequate.

Consider next contracts fixing damages equal to the *market charges* which the nonperformer would have paid had he marketed through the association. The damages are not likely to be as disproportionate as in the case above, but some overstatement of the actual damages incurred is inevitable unless practically all costs are fixed.

Let us turn last to provisions fixing damages at a *fixed absolute* amount. Potentially, this type of provision can be quite equitable. If the initial damages

provision equals the association's average fixed costs per unit, it will remain quite fair for some years despite changes in product prices. Thus, this method is less likely to result in inequities due to fluctuating product prices than is the fixed percentage method. This is not to say that inequities may not result. During periods of generally rising or falling prices, plant and other fixed costs will also change, eventually. Therefore such damages provisions should be revised periodically to insure equitability.

Of course, inequities may always arise if damages provisions are initially set too high or low. Some associations' damages provisions doubtless are higher than the "ideal" level, but some are also too low. All cotton contracts inspected set damages at $1.00 a bale. Yet average fixed costs are well above this level. Five dollars a bale certainly more closely approaches the actual damages suffered because of nonperformance.

Experience with nonperformance. In recent years few California coöperatives have collected liquidated damages from their patrons. Out of 218 responding coöperatives, 197 (90.4 per cent) indicated that from 1949 to 1953, inclusive, they had not recovered any liquidated damages from patrons. This indicates either that patrons of California coöperatives generally fulfilled their contracts, or else that coöperatives did not enforce their contracts in this way. Available data give no quantitative information on this point, but conversations with coöperative personnel suggest that the first reason is primarily responsible for the infrequent cases of liquidated damages.

Inspection of the 21 cases in which liquidated damages were paid suggests that high damages provisions successfully deter nonperformance. All but one of the coöperatives collecting damages had damages provisions of under 15 per cent of the 1953 market value of the commodity involved. The one exception involved an olive association with a damages provision of about 27 per cent of the market value of olives, and it recovered damages from only one member. On the other hand, the 20 associations having damages provisions under 15 per cent recovered damages from over 428 members. It is impossible to determine the exact number of patrons involved because four of the associations indicated only the amount of damages without stating the number of patrons involved.

Of the 45 California coöperatives in our sample having injunctions and specific performance provisions, only five used specific performance as a remedy for nonperformance. Four of these associations resorted to specific performance only once, and the other association twice. No coöperatives in our sample reported using injunctions as a remedy during 1949–53.

Although specific performance and injunctions are seldom used, these remedies may still be important. When a coöperative has a contractual obligation to deliver to a third party, liquidated damages from a patron may not give adequate relief. Often efficient operation demands that an association promise to deliver certain products long before members make delivery. Then if members do not deliver, the association may be unable to fulfill its own contracts. The damages it suffers then are greater than those suggested above. Not only are its per-unit operating costs increased, but it may also have to pay damages to its customers. Moreover, its inability to fulfill its promises may irreparably injure its reputation in the trade.

The great majority of dealers in the wholesale and retail trade are interested in adequacy and continuity of supply of products—especially of products sold under a trade or brand name. It may take a coöperative association years to build up a reputation for its products and its standing in the trade. The association could lose its reputation and its

standing if its volume fluctuated so greatly from year to year, due to changes in producer-patronage, as to prevent it from regularly supplying its dealer customers with the quantities of products they needed.

Because the extent of such damages cannot accurately be determined before an actual breach, the liquidated damages form of relief may be inadequate. It is in such cases that injunctions and specific performance are preferable forms of remedy. They insure the association of getting delivery. Therefore, associations having obligations of this type may, at times, find these remedies invaluable. This may explain why so many associations (40 per cent in our sample) include such provisions in their contracts. Although associations seldom have to use them, these provisions provide an added form of insurance against the damages suffered by nonperformance.

Payment of litigation costs. Most marketing contracts provide that if the association must bring a suit to enforce performance the patrons will pay the costs of such litigation. A typical litigation expense clause reads:

> The Member hereby agrees to pay all expenses arising out of or caused by such litigation and a reasonable attorney's fee to be fixed by the court rendering such judgement and the Association shall be entitled to the benefit of any lien securing payment of any such judgement.

Such a clause protects the association from being litigated into bankruptcy.

VI. IMPORTANT INTEGRATING PROVISIONS

Most discussions of coöperative marketing contracts deal only with their provisions regarding duration, delivery, and legal enforcement. While important, these provisions emphasize only one of the integrating functions of marketing contracts—that of delivery. This is certainly the contract's most important function in most cases. It binds otherwise independent farmers together by guaranteeing each of the others' performance. Emphasis on this function of marketing contracts has apparently led to neglecting the study of other functions, yet marketing contracts often can and do perform other important integrating functions besides insuring patron delivery.

As has been noted earlier, successful vertical integration of farm enterprises through the coöperative method is a complex process. It is much more difficult than when individual business firms expand vertically. When large numbers of farm businesses unite to form a jointly owned operation, it is very difficult to coördinate their production and marketing operations. Yet close coördination may be essential to marketing efficiency for the group. As previously mentioned, when farmers form a coöperative, they must relinquish to it some sovereignty over certain of their production and marketing decisions.

The extent of such subordination depends in part on the amount of coördination between patrons and their association necessary to insure operating efficiency. This depends largely on the peculiarities of the commodity the coöperative markets, the nature of the marketing functions it performs, and the character of the markets in which it operates. For example, single-function associations may require little coördination. A livestock association whose only function is to sell need not be closely integrated with its patrons. When associations perform many complicated marketing and processing functions, however, they may have to be closely integrated with their patrons.

Today, more and more associations perform more than a single function. In the following pages, we will look at various types of coördinating or integrating provisions included in California marketing contracts. We shall analyze them

so as better to understand their function. Finally, on the basis of our findings, we shall try to develop some principles to guide associations using marketing contracts.

Delivery and acceptance provisions. Coöperative marketing contracts may perform many integrating functions. But their primary integrating purpose is to bind patrons to deliver part or all of their crop to their coöperatives during a specified period of time. As pointed out earlier, if members are not so required to patronize their association, coöperation may be a weak and often ineffective form of vertical integration. But when members must market through the association for a period of time, they become closely integrated with it. They are then, in fact, an integral part of the association, and its management, assured of their continuing participation, can plan accordingly.

The delivery and acceptance provisions of an association's marketing contract are the legal basis of such integration. They spell out the legal rights and duties of all association members in this respect, as well as those of the association to its members.

Delivery provisions. Nearly all California coöperatives using contracts require patrons to deliver all of a particular commodity owned or controlled by them. Usually the contract excludes that part of a commodity consumed on the farm. However, local dairy associations of federated coöperatives typically are directed to market all of their milk products through the central except those sold in their "local market." Citrus locals are not given this right. In this study, "total delivery" clauses refer to a patron's obligation to deliver his entire crop not consumed at home, as well as to local dairy associations compelled to market through their central associations all products not sold in "local markets."

All but 14 of the 117 marketing contracts analyzed included total delivery provisions (table 6). The following are typical total delivery provisions included in California marketing contracts:

> . . . it shall be the duty of each member of the Association, and each member agrees to deliver to the Association for packing and marketing . . . all fruit matured during membership upon the member's lands. (Citrus association)
>
> . . . the grower agrees to deliver to the Association at its ginning plant . . . all cotton produced by or for him or acquired by him as landlord or lessor to be ginned by the Association. (Cotton gin)
>
> It shall be the duty of each member of the Association . . . to deliver to the Association for processing and marketing, and to market through the agency of the Association all of the milk and cream produced by the cows of such member during membership. (Dairy association)

Eight coöperatives not requiring or permitting total delivery of their patron's marketable crops were wineries. These associations require patrons to deliver specified absolute amounts of grapes (expressed in tons or acreage) rather than their entire crops. The six other associations not requiring or permitting total delivery were prune dryers.

Acceptance provisions. Just as nearly all patrons must deliver their entire crops, so must most coöperatives accept delivery of their patrons' entire crops. Only 21 (17.9 per cent) of the 117 contracts inspected included specific provisions permitting coöperatives to limit the amount of their patrons' crops which they would market (table 6).

Provisions permitting limited acceptance due to "Acts of God" were not included in this count. In fact, many coöperatives include such provisions in their marketing contracts. A typical provision of this type reads:

> In the event that either party to this agreement be unable to perform by reason of strikes, lockouts, fire, explosion, war, Act of God, or other happenings or cause, beyond the reasonable control of such party, performance hereunder by such party shall be excused as long, but only so long and to such extent as performance be prevented thereby.

Table 6. Selected California Coöperative Marketing Contract Provisions Integrating Growers with Their Coöperative

	Citrus	Wine	Other fruits and vegetables	Field crops	Dairy products	Poultry products	Nuts	Total all types	Per cent of total number in sample
	Number in sample								
Total coöperatives with contracts	33	9	40	10	5	4	16	117	100
Contract provisions:									
Total delivery	33	1	34	10	5	4	16	103	88.0
Limited acceptance	0	8	10	0	2	1	0	21	17.9
Quality standards set	32	9	28	2	5	4	1	81	69.2
Harvest standards set	31	0	17	0	0	0	0	48	41.0
Coöperatives may harvest crops	27	0	2	0	0	0	0	29	24.8
Delivery time set	32	9	23	3	2	1	1	71	60.7
Crop inspection	3	0	7	0	1	1	0	12	10.3
Crop pooling	25	9	28	3	4	4	16	89	76.1
Crop-size report	0	0	10	1	1	0	1	13	11.1

Fourteen of the associations including limited acceptance provisions were the above-mentioned wineries and prune dryers. The wine associations establish specified amounts of various grape varieties which they will accept from members each year. Members cannot deliver more or less than such specified amounts without the special approval of the association. The amounts to be marketed are usually agreed to annually or when contracts are renewed.

Prune-drying associations need accept from members only amounts equal to the drying space they contract for, and members must supply up to this amount if available. Members having more prunes than can be dried in the space they have contracted for must dry them elsewhere if the association requests them to do so.

The limited acceptance provisions in the contracts of the other seven associations (marketing turkeys, eggs, beans and rice, olives, deciduous fruit, figs, and dairy products) permit the association to limit, when necessary, the amount it will market for its patrons. Such limited acceptance clauses are usually accompanied by "prorate" clauses requiring that all patrons be treated alike when their coöperative decides not to accept total delivery. The following are further examples of limited acceptance clauses:

. . . the grower shall sell to the Corporation each and every year after the date of this agreement, such number of tons of grapes as may be agreed upon from time to time between the Corporation and the grower, it being understood and agreed that the grower shall have the privilege of selling and delivering to the Corporation from time to time such proportion of all the grapes which the Corporation shall, from time to time, decide to accept and receive as the number of shares of stock held by the grower shall bear to the total issued and outstanding stock. (Wine association)

The association reserves the right to prorate the delivery of tonnage agreed to be delivered by the grower, and, if necessary in the sole discretion of the association, to reduce the tonnage agreed hereby to be delivered, so long as the tonnage shall be prorated with other growers equitably. (Fig association)

The producers agree, notwithstanding any other provision herein, upon notice via registered mail, to accept as an enforceable condition of this agreement, any *maximum* quota for delivery of milk under this agreement, which shall be established, as needed, by the Board of Directors. (Dairy association)

When should associations limit acceptance? Although most California coöperatives do not limit the amount members may deliver annually, some do. Under what circumstances, then, should coöperatives set quantity limits?

The correct answer to this question depends on a number of things. The most important of these are: the objectives of the association; the character of its marketing facilities; and the nature of the market in which it sells its processed products.

First, how does the nature of an association's marketing facilities affect this matter? If an association has very flexible marketing facilities there may be little need to limit the amount of products members market through it. For example, associations acting simply as the broker or agent of farmers in selling their products generally do not have to limit the amount they market for members. (Of course, efficient operation may require that members market exclusively through their association.) A livestock association representing members in an auction or other market can change its volume of operation from month to month, week to week, or even from day to day, with relative ease. It can do so because in its operations there are few "fixed" factors which rigidly control its scale of operations.

But all types of associations obviously do not enjoy such operating flexibility. Most California coöperatives perform one or more processing functions; and because processing involves plant facilities and equipment of various sorts, such associations have some fixed factors which may limit the scale of their operations in the short run. Although all processing plants have some fixed factors,

they may still have very flexible operations. For example, a fruit-packing plant can vary its operations by changing the number of workers employed at a given time, by changing the length of hours worked by a given labor force, or by increasing the number of shifts. Most other processing plants have similar flexibility. And although temporary plant gluts may still develop, once a plant reaches its peak capacity, such gluts may be reduced by controlling members' harvesting and/or deliveries. Such action seldom involves actual control over the amount members market through their association in a given season; rather, it involves modifying the delivery time of their supply (see page 41).

If a plant is extremely inflexible as to the amount it can handle during the season, and if the above method of modifying supply is impossible, an association may find it necessary to set absolute limits on the amounts members market through it each season.

Next, how may the competitive nature of the market in which coöperatives sell require them to set limits on members' deliveries? Suppose, first, that an association sells in a perfectly competitive market, that is, one in which it can sell unlimited amounts at prevailing market prices. If such an association's marketing facilities were also completely flexible, it would not have to set limits on the amount members could market through it because the association would get the same price for each unit it sold for its members.

But suppose an association sold in something less than a perfectly competitive market—that is, one in which it could not sell unlimited amounts at going market prices. This would come about because an association "differentiated" its product through advertising or otherwise. This might enable it to get a premium price for its product, but obviously it could not sell unlimited amounts at such premium prices. Therefore, it could maximize its members' profits only by limiting the amount they sold through their association. One way of accomplishing this would be to specify annually the amount members could market through it. Otherwise, members might expand their production until the association would be unable to sell all of their products at premium prices, thus defeating the purpose of its product-differentiation program.

Thus, the advisability of limiting delivery turns largely on the flexibility of an association's marketing facilities and on the competitive character of its markets. How do California associations fare in these respects?

We have not here studied the flexibility of California coöperatives or the nature of the markets in which they sell. But familiarity with California associations suggests that the bulk of these do have quite flexible processing and marketing facilities and do sell in highly competitive markets.[13] Insofar as this is true, it follows that most associations are following sound economic policy in not limiting their members' deliveries. However, some associations do limit deliveries and apparently have sound reasons for doing so. Let us look at the associations in our sample which most commonly place some

[13] It should not be inferred that merely because some California coöperatives market a large proportion of the total supply of some crops they have significant long-run market power, that is, face an inelastic demand. Coöperatives acting alone are unable to control the total supply of particular agricultural products. Even if a coöperative does successfully control the supply of its members, it cannot control that of nonmembers. Consequently, even when an association markets a large share of total supply, it is usually forced to behave very similarly to firms selling in very competitive markets. As we saw above, such associations may gain nothing by limiting members' deliveries. The discussion in the text applies most directly to associations selling differentiated products. When you differentiate your product, you are, by definition, selling a product that no one else sells. Then, by controlling your supply, you are able to exercise some control over price.

restraints on the amount of products they will handle for their members—prune dryers and wineries.

The amount of prunes that a prune association can handle each year is limited by two factors. One is the relatively short harvesting period after which the crops must be dried as soon as possible. The other is the inflexible drying process; once all dehydrators are filled, the plant's capacity cannot be increased nor can the drying period be speeded up.

This combination of factors definitely limits the volume of prunes that can be dried each year by plants with a given fixed investment. Associations must therefore annually limit the amount they handle for each member. No long-run limitation need be imposed in this case. Fixed plant can be expanded quite easily from year to year, so if members' acreage increases or new members are added, additional capacity can be built before the next crop. Thus, the short-run inflexibility of the association's processing facilities is chiefly responsible for limiting members' deliveries.

Eight of the nine wine associations in our sample also limit delivery, but apparently for other reasons. Here it is not only inflexible plant capacity but also the character of demand that encourages them to limit members' deliveries.

Wineries (both coöperative and noncoöperative) probably do not make very large long-run noncompetitive profits, for the large number of firms in the industry and the ease of entry makes this an effectively competitive market. Some individual firms, however, may face an inelastic demand for their products. This results from product differentiation, which enables them to sell their products above bulk-wine prices. However, because they cannot sell unlimited amounts at premium prices, the amount members market through their associations must be limited; otherwise, they might often be forced to operate at other than optimum outputs.

Wineries also have an incentive to control acceptance because their plants are relatively inflexible in the short run. Because the wine-aging process requires time, available storage space always fixes an upper physical limit on output.

These two factors in combination may make it imperative for wineries to control their volume. To do otherwise might cause them to operate very unprofitably in many years. Understanding of these basic economic conditions makes it clear why nearly all California coöperative wineries have included limited acceptance provisions in their marketing contracts. They are following sound economic procedure in doing so.

Today these factors are not always important to all California coöperative wineries. Because many are operating well under capacity, there is little likelihood of their plants' being glutted in the near future. Because many do not sell differentiated products, they need not control their supply for the market reasons mentioned above. However, some associations do have long-term contracts with noncoöperative marketing firms. When these call for the delivery of specific amounts of wine each year, an association may have a definite need to limit members' deliveries. But if such contracts simply specify delivery of an association's entire output to a buyer, the association need not limit members' deliveries. The one association in our sample that does not have a limited acceptance provision has such an outlet for its wine.

However, associations that have successfully differentiated their products have found it necessary to limit members' deliveries in order to reap maximum benefits for their members.

Quality-Control Integration Provisions

An important factor determining the net revenue coöperatives are able to return to patrons is product quality. Much

of a product's quality is determined by the skill and care exercised by the association in processing and marketing. In many agricultural products, however, the quality of the end-product sold by the association, whether processed or not, is determined largely at the farm level. Therefore, maximization of the association's net returns may require that the association control some of its individual growers' production practices.

Many California associations recognize these facts. They have inserted a variety of quality-control provisions in their marketing contracts. Most frequently these include: (1) setting quality requirements; (2) setting harvesting methods; (3) harvesting of patrons' crops by the coöperative.

Quality requirements. Practically all coöperatives exercise some control over product quality, and about two-thirds of the contracts inspected specifically gave the association such authority (table 6). Some coöperatives go further than others in this respect. For example, in one dairy association the Board of Directors may "from time to time establish proper rules and regulations for the feeding, milking and caring for dairy herds." A winery's marketing agreement states:

> The Association reserves the power to set standards of maturity, quality and sugar contents which must be met by all grapes delivered by the grower, and to provide reasonable penalties for differences therein.

Harvesting requirements. Many fruit and vegetable associations go beyond setting quality requirements. They frequently establish harvesting and handling practices as well. This insures that patrons will deliver products of the necessary quality.

Practically all of the citrus associations and about one third of the other fruit and vegetable associations in our sample permit the association to set harvesting requirements (table 6).

Harvesting of crop by association. In the citrus industry (and to some extent in deciduous fruits and in vegetables) many associations go a step further. They actually arrange for the harvest or perform it themselves. About 80 per cent of the citrus associations in our sample are legally permitted to perform this function (table 6). A typical provision giving authority to an association to harvest its patrons' crops reads:

> The picking, hauling, selling and marketing of said citrus fruit shall be done by the Association or under its direction in accordance with rules and regulations of the Association.

Sometimes associations harvest their members' crops because they can do so more economically and efficiently than the members can. This occurs if specialized harvesting machinery is needed which requires very intensive use to pay for itself. For example, a coöperative processing fruits and vegetables owns spinach-harvesting equipment because its members cannot efficiently operate their own, either because of the size of their crops or because they do not grow spinach every year.

Why control quality? Quality-control provisions have two chief objectives. First, they aid individual patrons in getting a higher-quality product to the market. Second, they protect patrons from being harmed by the delivery of inferior products by some patrons. Coöperative associations whose chief objective is the maximization of members' income may properly concern themselves with both objectives, although the latter is more important from the viewpoint of the entire association, and most quality-control provisions are apparently directed toward it.

For example, grape quality is extremely important to wine quality. If some patrons use cultural and harvesting practices resulting in poor-quality grapes, pooling of their grapes with those of other members might result in a low-

quality wine. Thus, all members could be harmed by the practices of a few. To avoid this, wine associations can set grape maturity, quality, and sugar-content requirements.

In citrus, decay is a great enemy of quality. Decay is caused by blue and green mold spores, which cannot penetrate healthy fruit (Gardner and McKay, 1950, pp. 30–31). If the fruit's skin is damaged, however, the spores are able to enter and start the decay process. Because skins are easily damaged during picking, skilled and careful pickers must be employed. Pickers must wear gloves, use special clippers, and cut rather than pull the stem. These and other precautions must be taken to prevent fruit damage. Most California citrus coöperatives have met this problem by taking over the harvesting job for their patrons. Thereby they insure a final product of the highest possible quality.

Timing of Delivery

Efficient operation of many coöperatives requires more than assurance that a given quantity and quality of a product will be delivered during the year. *Timing of delivery* may also be important for various reasons. Perhaps most frequently, timing of delivery is necessary to keep a coöperative's processing, storage, or other facilities from being periodically operated over or under capacity. In other cases, delivery time is important because the coöperative itself has an obligation to deliver at some particular time. Finally, for an association to maximize its patrons' returns, it may also have to control delivery in order to prevent temporary market gluts or to take advantage of temporary shortages.

For these and other reasons, successful member-coöperative integration requires the member to give up his control over delivery time. This decision must be made in the best interests of the entire association.

Many California coöperatives recognize this fact and include specific provisions in their contracts giving this right to their association. A typical provision insuring delivery at the association's discretion reads:

> The time or times when fruit shall be picked for marketing shall be determined in accordance with general rules to be established by the Board, which rules may be changed from time to time.

Of the contracts inspected, 71 (60.7 per cent) give associations a legal right to set a specific delivery time (table 6). All but one citrus association and over half of the other fruit and vegetable associations in our sample have such a provision. Of the other associations, only six in our sample—one nut, two field crop, one poultry, and two dairy associations—have a legal right to set delivery time. Other associations have provisions requiring delivery before a particular date. These have not been considered here because they are less important in regard to integration.

Associations marketing some products need not fix delivery time because patrons must deliver within a relatively short period in any event. Since dairy and poultry products, for example, must be delivered fairly quickly to prevent spoilage, no legal obligation setting delivery time may be needed. But some associations whose contracts do not fix delivery time should legally be able to do so.

About 40 per cent of the marketing contracts inspected did not give coöperatives control over delivery time. Nevertheless, many of these associations probably can legally set delivery time. Bylaws of many associations give the directors and officers quite broad discretion in marketing patrons' crops. Such discretionary powers may well give associations power to specify delivery time. We have found no legal cases setting forth the limits of a coöperative's rights in this respect.

Crop inspection. Judicious setting of delivery time and establishment of control over quality require the coöperative to have quite specific knowledge of its members' crops—their volume, quality, and state of maturity. Some associations make certain they receive this information by giving the association the right to inspect patrons' production operations. Only 11 (10 per cent) of the contracts in our sample included such provisions. Ten of these were fruit and vegetable associations. The other was a turkey egg association.

The following clause from an avocado association's contract gives it the right to specify delivery time and also to inspect members' crops (this contract also includes a provision requiring members to report an estimate of their yields on request):

> The time, place, manner and quantity of delivery of avocados to Calavo are to be directed by it in order to enable Calavo to properly receive, pack and market the fruit of all its members. Calavo shall have the right, at reasonable hours, to inspect members' groves for the purpose of crop estimate and inspection.

Coöperatives may have a legal right to inspect crops even when it is not specified in the contract. The courts probably would rule that this right is implied in provisions giving associations the right to set delivery time and to harvest patrons' crops. (If this is the case, nearly all citrus and most other fruit and vegetable associations have this right.) Even so, it may be advisable to include such a provision for the patrons' information.

Pooling and Grading Provisions

Very often efficient processing, storing, and selling require product pooling, that is, commingling by an association of its patrons' products. (Coöperatives also apply the pooling principle to patron expenses and returns.) By giving their association the legal right to pool, patrons permit complete physical integration of their products.

Of the contracts inspected, 89 (76.1 per cent) give the association a legal right to pool its patrons' crops (table 6). These provisions permit several types of pools. Most frequently mentioned are pools by quality and time. Quality pools insure that members will receive payments reflecting differences in market conditions at different times of the year. For example, the first strawberries of the season usually command a relatively high price. Therefore, strawberry associations ordinarily establish separate pools during the season to reward early producers.

A usual concomitant of product pooling is the averaging of returns to growers. Under the pool principle, each grower contributing products of like quality to a particular time pool receives the same return per unit. This has the advantage of spreading price risks over the pool participants. Of course, it also has the disadvantage that it may decrease some patrons' returns. As noted earlier this possibility may at times encourage some patrons to market outside their association. Then, only the total delivery clause of the marketing contract may insure patron performance.

Because pooling requires commingling of products of like quality, coöperatives must devise grading systems. Eighty-one (69.2 per cent) of the contracts inspected gave coöperatives the right to establish grading systems. Some associations reserve exclusive rights to set up and interpret such grades to prevent grading disputes from causing poor member relations; others provide for arbitration in case of disagreement. A typical provision of the latter type reads:

> Any dispute over quality shall be settled by arbitration. Each party shall appoint one arbitrator and said arbitrators shall jointly select a third and the decision of the majority of said arbitrators shall be binding upon the parties. All expenses of the arbitration shall be borne by the party against whom the decision shall be rendered.

Crop Size Reports

Coöperatives must make many planning decisions before members deliver their crops. They must often build to increase capacity. They must hire employees. They must often contract with third parties. They may have to estimate the market price of the coming crop.

Accurate decisions on such matters require knowledge of future crop volume. Total delivery contracts give some information on this score, but not enough. They only tell how many patrons will deliver their crops in a given year. But the association must also know something of the crop size of its patrons. Past crop sizes are not necessarily adequate guides because crop sizes of individual patrons may vary from year to year. Also, patrons may buy more land or sell some of their farm land. They may shift from one crop to another. Their yields per acre may vary greatly each year. For efficient operation the association must be kept closely informed of such changes.

Many coöperatives realize this. Some feel that this information is so essential to efficient integration that they have given it a legal basis in their contracts. Thirteen (11.1 per cent) of the contracts inspected require their patrons to report the size of their operations from time to time (table 6).

There are two types of crop-reporting provisions: one requires patrons to report the yield of their current crops; the other requires a report of any change in acreage from one year to the next.

Provisions of the former type, permitting the association to plan ahead for the disposition of current crops, are in the contracts of eight associations (four marketing beans and one each marketing figs, peaches, nuts, and avocados). The following almond association's crop-report clause is typical:

As soon as the fruit has formed upon the tree each year and whenever thereto requested by the Manager of the Exchange, the Member agrees to mail to the Exchange ... an estimate of the yields of almonds covered by this contract, and also, each year immediately upon the harvesting of such almonds to mail to the Exchange a statement of the amount of such yield.

Six associations (three olive and one each marketing avocados, hay, and dairy products) require their patrons to report changes in acreage or number of livestock. In contrast to current crop-size information, this information is useful for longer-term planning. The following acreage-reporting provision of a hay-marketing association is typical:

It shall be the duty of each member, and each member agrees, promptly to notify the Association in writing of any change in hay producing lands of the member within the market district resulting from the acquisition of additional lands or the disposition of lands theretofore farmed.

Other Marketing Contract Provisions

California coöperatives use a variety of contract provisions in addition to those already discussed. Some of these reflect other problems in successfully integrating patrons with their coöperatives. Others are common to any contract involving transfer of ownership or the granting of agency. The following provisions are most often found in California coöperative marketing contracts in addition to those treated above. We have not enumerated the frequency of all of these provisions.

Association's independence of control. Coöperatives exist and operate for the benefit of their farmer-owners. For efficient operation, however, they should not be subject to too much interference from individual patrons. Once the association elects its board of directors, the board and its appointed management must have the right within the framework of broad policy decisions to pursue what they think is a desirable course of action. They must be able to handle and market their patrons' crops without continual interference from in-

dividual members. Simply put, their control over operations must be independent of the actions of individual members.

Without such independence, coöperation would often be an unworkable form of integration. Each patron could continually make demands regarding the way he thought things should be done. To prevent this, many coöperatives include in their bylaws provisions requiring patrons to give up control over their association's operating policies. Some place special emphasis on such independence in matters pertaining to marketing by including appropriate provisions in their marketing contracts.

This does not mean, of course, that members have no voice in management policy. On the contrary, each time they elect their board of directors, they express themselves indirectly in this respect. Moreover, if the board of directors ignores the desires of an important segment of the association, it faces the risk of losing its patronage. This threat may force consideration as well of the demands of a small minority which could not hope to force such recognition through the election process alone.

But although the patrons ultimately exercise much control over management policy, independence-of-control clauses give an association's management a free hand in following its day-to-day operating policies. The following clause from a dairy association's marketing contract gives it such "independence of control":

> All matters pertaining to the handling and marketing of products shall be transferred solely in the name of the Association, or in the name of any agent or agency to or through which said products may be consigned or shipped for marketing or ultimately marketed. ... No member by virtue of being the owner of, or having furnished any products, shall exercise any control over the Association in regard to either handling or marketing said products, or the conduct of the business of the Association. In all of such matters the Association may in good faith use its own discretion and judgement, free from any direction from the member furnishing the products.

This particular contract is an agency contract. But some associations insert independence-of-control clauses even when they use purchase-and-sale contracts. For example, a hay association that uses a purchase-and-sale type of marketing contract includes the following clause:

> No member by virtue of having been the owner of, or having furnished any hay shall exercise any control over the association in regard to either the marketing of said hay, or the conduct of the business of the Association, in all of which matters the Association may, in good faith, use its own discretion and judgement, free from any direction from the member furnishing the hay.

Such clauses may be included either in an association's bylaws or in its marketing contract. But because they emphasize the fact that growers relinquish control over their products after delivery, they might most properly be included in the marketing contract. They would then be with the other provisions spelling out the member's duties and rights in marketing his crop.

The coöperative method of operation. An important and integral part of all marketing contracts between an association and individual members is the basis on which members will contribute to the capital needed by the association and to its operating expenses. These financial arrangements are spelled out in detail either in the bylaws or in separate marketing contracts or in both. These financial arrangements vary considerably between associations handling different products or performing different services, and also sometimes between associations performing similar services.

In general, marketing contracts specify that members contribute to the capital needed by an association pro rata to patronage, that is, according to the use each member makes of the services rendered by the association. Special provisions are usually included in contractual documents to ensure the separate

identity of the equity of each member in the net assets of the association.

Members also contribute to the annual operating expenses of the association on the basis of patronage. Coöperatives conduct their affairs on the "operation-at-cost" principle. Again, specific provisions are made in the contractual documents whereby any operating overages (the excess between deductions for expenses and actual expenses) will be prorated back to members at the end of a fiscal year. The association, as such, will not make any profit. The excess of operating income over operating expenses at the end of a fiscal year may be returned to members either as a prorated patronage refund or as a prorated addition to the capital contributed by members.

Such provisions leave no doubt as to the coöperative's financial obligations to its members (and in some instances also to nonmember patrons). They guarantee equitable treatment to all patrons. The following clause appearing in the bylaws of a dairy coöperative is typical (except for minor differences in wording) of clauses pertaining to operating costs:

> Section Four—Non-Profit Character. The general purpose of this association is to serve as agent for its members at cost, pro-rated according to volume and value of business done; and in accordance therewith its business and operation shall be conducted at all times without profit to the association as such and upon a non-profit cooperative basis, for the primary benefit of its members, turning back to them all proceeds less incurred expenses on a proportionate volume or value basis. To this end, all proceeds from the sale of members' products less only the Association's expenses, are hereby expressly declared and acknowledged to be the property of members whose products are so sold.

Marketing function coöperative is to perform. It is a common practice for marketing contracts to spell out the type of processing or other marketing functions which the coöperative is to perform. Such clauses leave little doubt as to the marketing functions the association is to perform for its patrons. On the other hand, they also assure the patron that his products will be handled in a particular way or processed into a particular product.

The following clause from a winery's marketing contract is typical of the broad discretionary power given to the association's management in marketing members' crops:

> The Association agrees to manufacture such grapes together with the grapes delivered by other growers into wine, brandy or such other products as the association may determine . . .

Industry marketing agreements. Many of California's perishable agricultural products have been, or are now, marketed under industry marketing agreements or orders. The main purpose of these government-regulated programs is to stabilize farm product prices through orderly marketing. These programs are permitted by both state and federal legislation. The major laws affecting California farmers are the Agricultural Marketing Act of 1937 and the California Marketing Act of 1937.

Before marketing agreements can be instituted, they must be assented to by a certain percentage of the producers. Under federal marketing orders, two-thirds (for California citrus and individual-handler pools in milk it is three-fourths) of the voters in a referendum must approve the order. Under the California Marketing Act, there are three ways of obtaining approval: (1) by written assent of 65 per cent of the total producers of the product covered by the order, who also produce at least 51 per cent of the product; (2) by approval in a referendum by 51 per cent of the total producers of the product, and by producers who produce 65 per cent of the product; and (3) by approval in a referendum by 51 per cent of the producers of the product, who also produce 51 per cent of the total product. The California Director of Agriculture determines whether approval should be given by written assent or referendum.

Both the Federal and State Marketing Acts, however, permit a coöperative to give the approval of all of its members when authorized by them to do so. The California Marketing Act reads:

In finding whether such marketing order is assented to in writing or approved or favored by producers, the director shall consider the approval of any nonprofit agricultural cooperative marketing association, which is authorized by its members so to assent, as being the assent, approval or favor of the producers who are members of, or stockholders in, such nonprofit agricultural cooperative marketing association.[14]

The Agricultural Adjustment Act as amended, reads as follows:

Whenever . . . the Secretary is required to determine the approval or disapproval of producers with respect to the issuance of any order, the Secretary shall consider the approval or disapproval by any cooperative association producers, bona fide engaged in marketing the commodity or product thereof covered by such orders, or in rendering services for advancing the interests of the producers of such commodity, as the approval or disapproval of the producers who are members of, stockholders in, or under contract with, such cooperative association of producers.[15]

When a farmer gives such authority to his association, he, in effect, agrees to abide by the majority decision of the association on the question of industry marketing agreements. This gives the association a stronger voice than it otherwise would have. It permits an association's directors to speak and act as the representatives of the entire association on these matters.

The individual farmer's agreement partially to relinquish his power over this decision is another important form of integration. But in principle it is no different than when he agrees to let his association establish quality, delivery, or other requirements affecting his production or marketing. He relinquishes his rights over such decisions because he believes this will result in greater overall operating efficiency, which in the end is to his economic benefit. Furthermore, an association's directors are not likely to vote for an agreement unless they believe the bulk of the members favor it. Otherwise, they run the risk of stirring up membership dissatisfaction. Very often associations poll their members at annual meetings or in other ways to find out how the membership feels on an impending marketing agreement or order.

How many California coöperatives are integrated in this way? Our available evidence does not permit a very accurate estimate on this score. For although this is essentially a marketing contract provision, apparently few California coöperatives include it in their marketing contracts. Of the fruit, vegetable, nut, and dairy marketing contracts inspected, only three include such provisions. The other types of associations in our sample do not handle products affected by state or federal marketing agreements.

Such provisions in marketing contracts are rare not because the coöperatives fail to use them but, rather, because this authority is generally included in the bylaws, among the powers of the boards of directors. We inspected the bylaws of 34 fruit, vegetable, and dairy associations, 18 of which gave the associations' boards of directors the discretion to assent to marketing orders on behalf of their members. These consist of 8 of the 20 citrus associations, 9 of the 11 other fruit and vegetable associations, and 1 of the 3 dairy associations. (We did not inspect any nut association bylaws because those in our sample use separate marketing contracts.) This small sample suggests that more than half of such associations give their directors this authority.

A typical bylaw clause gives the directors the following powers:

To assent in writing or otherwise, on behalf of the members of the Association and all producers of fruit marketed or to be marketed by

[14] Agricultural Code of California, revised to Sept. 9, 1953, 1300.16 (3).

[15] Public Law No. 320–74th Congress, section 80 (12).

Association to any marketing order or amendment thereto pertaining to and regulating, directly or indirectly, the marketing of fruit marketed by Association, made or proposed to be made by a commission, committee, individual, government agency or officer, pursuant to any present or future law of the State of California or of the United States including, but not limited to, the California Marketing Act of 1937, as amended, and the Agricultural Prorate Act of California (Chapter 754, Statutes of 1933), as amended. By the foregoing provisions, the members of Association intend, among other things, to authorize Association to assent to marketing orders on behalf of such members, as producers, as such assent is referred to and provided for in Section 1300.16 of the Agricultural Code of California.

Whether or not such authority should be included in an association's bylaws or its marketing contract is largely a matter of preference. Legally, it makes no difference. The California law simply requires that the association show proof of its authority to act for its members in this respect. The United States Marketing Law does not require such proof. It seems, however, that such provisions would be more appropriate to the marketing contract, where several associations have put them. This has the advantage of placing them with other important legal provisions integrating the marketing activities of the association.

Method and time of payment. Most contracts include payment provisions of one sort or another. Of the contracts inspected, 87 (74.4 per cent) included specific payment provisions. Frequently these provisions call for the association to make a payment at the time of delivery or shortly thereafter. For example, a raisin coöperative's contract reads:

Ten days after the receipt of said raisins by Buyer [Association] at the place mentioned above, Buyer agrees to make Seller as large an advance per pound therefore as in its judgement financial and market conditions will justify.

A subsequent provision of this association provides:

Progress payments in due proportion shall be made as respects each pool from time to time as rapidly as in the judgement of Buyer it is practical to make such payments and such payments shall be continued from time to time until the accounts of each pool are fully settled.

Termination and Rejoining Provisions

All but 10 of the 117 contracts in our sample include provisions setting forth the way in which patrons can terminate their contracts. These usually are part of the "duration" clause. But only 59 (50.4 per cent) spell out the way in which the association can cancel the contract or refuse to renew it.

Quite frequently contracts also include a clause setting forth the conditions for rejoining a coöperative after a patron leaves it. Usually these require a waiting period of one year and the consent of the board of directors.

Customarily, termination clauses also spell out the association's duties concerning the repayment of the grower's investment in the association.

The following "termination" clause of a bean association includes all of the items mentioned above. It is quite typical of California contracts.

This Agreement and Membership in the Cooperative may be canceled and terminated by any signer hereof, not indebted to the Cooperative, by notifying the Secretary of the Cooperative in writing prior to June 1st of any year. The effective day of cancellation and termination will be the 1st day of January next following receipt of such notice. The member withdrawing in accordance with the provisions hereof shall be paid the amount contributed by him as a Membership fee within sixty (60) days after the effective date of such withdrawal. Such Member shall also be paid the amounts contributed by him to the Revolving Fund at the time or times as same would have been paid had he continued as a Member. Any Member so withdrawing shall not be eligible to be a Member again until the next year following the effective year of his withdrawal and then only by a vote of the Board of Directors of the Cooperative.

In this connection the bylaws of some associations provide for the expulsion

or cancellation of membership of members who do not comply with certain conditions. For example, the bylaws of a poultry association provide that:

The Board of Directors shall have authority to, and may, cancel the membership, and/or expel, a member for the reasons and subject to the procedures outlined herein.

Following this are several paragraphs that give the reasons for termination or expulsion and the procedures to be followed. One of the reasons for termination would be failure to patronize any department of the association in the minimum amount of $100 in any one year. Members are assured of the right of hearing before termination or expulsion.

This type of provision is frequently written into bylaws because an association has certain minimum expenses in connection with record-keeping even for members who are no longer active. In an industry like the poultry industry, where there is a relatively heavy turnover among poultrymen, it gives an association an opportunity to eliminate from its membership persons no longer actively engaged in poultry production or who in other ways are not using the facilities of the organization.

Transfer of obligation to perform. In most fruit associations (and in several other types), at time of joining or when they sign a marketing agreement members are required to designate the land or lands from which they will be obligated to deliver fruit. They are, however, relieved of such delivery obligations should they make a bona fide sale of any portion of such lands—provided they give written notice of such sale to the association.

The bylaws or marketing agreements of many fruit-marketing associations, however, provide for the transfer of delivery obligations if land of a member is transferred in any way other than by bona fide sale—for example, by gift or death of a member. The following is a typical provision in such cases:

. . . the obligation of the member in respect of the fruit produced on the transferred lands which was existing immediately prior to such transfer, shall continue and run with such fruits and the lands on which grown and shall represent a right therein of the association, and such obligation shall be binding upon the successor of interest or transferee; and such fruit and the transferred lands shall vest in and be held by the transferee or transferees, including any personal representative, heirs, legatees, devisees, surviving joint tenant receiver and trustee in bankruptcy, subject to the same rights and obligations as existed immediately prior to the transfer, but also subject, nevertheless, to the right of withdrawal by such transferee or transferees upon the notice, at the time, and in the manner provided in Section 4.01 (c).

Guarantee of control. Many contracts include a clause requiring that the patron actually have control of the crop in question. A typical "control" clause reads:

This grower expressly warrants that he is now in a position to control said crops and would be able to deliver according to this agreement; and that he has not heretofore contracted to sell, market or deliver any of the said (crop) to any person, firm or corporation. If he has so contracted, he shall so state at the end of this agreement; and any crops covered by any such existing written agreement shall be excluded from the terms hereof to the extent and for the time then indicated.

Such clauses are designed to protect the association against double contracting. They make it clear to a grower that he should contract for only that part of his crop not already contracted to someone else.

VII. HOW MUCH INTEGRATION IS DESIRABLE?

The preceding discussion demonstrates that California coöperatives include a variety of integrating provisions in their marketing contracts. The question is, to what extent should the production, harvesting, and marketing activities of individual patrons be integrated with those of the entire association? The answer to this question differs, depending on the assumptions we make about the objectives of coöperative associations. If their objective is to maximize their patrons' net revenue, the chief guiding principle is clear: Patrons should relinquish particular production or marketing decisions to their association when such integration promises significantly greater long-run operating efficiency for the association as a whole. For if it does, net returns of patrons on the average will be increased.

Many California coöperatives do, in fact, use integrating devices to insure greater operating efficiency. Most frequently these involve provisions affecting product volume, quality, delivery time, and pooling. But if control of these revenue-affecting factors is so important, why do not more associations use them? There seem to be at least four important reasons.

First, not all of the above-mentioned forms of integration are important to all coöperatives. For example, harvesting methods are extremely important to quality in fresh fruits, but they are less important in nuts. Or when an association does not pool its patrons' products, as in livestock, the association as a whole may be unaffected by the quality of an individual member's products. Therefore, close integration on matters of quality is not important to efficient operations.

Second, in some cases, fuller integration may cause grower dissatisfaction. For example, it may be desirable from the revenue standpoint of most members for an association to have strict quality control over patrons' production or harvesting. If an important minority objects to such action, however, the association may forego strict quality control in favor of greater membership harmony. For example, it has been known for many years that the washing of eggs reduces their keeping quality. A large poultry association in California carried on an educational campaign among its members for several years before introducing a quality-control program under which members received a lower price for washed than for unwashed eggs. At present nearly 100 per cent of all eggs received from members are unwashed.

Failure to adopt a particular integrating provision in this case may or may not have been due to the abandonment of the profit-maximization principle. If operations are modified simply to increase some members' "satisfaction," the profit principle probably has been abandoned. The association may have abandoned it in favor of some other principle, such as general membership harmony. But if the majority is willing to modify its operations because such dissatisfaction would be reflected in lower operating efficiency (due, for example, to lower membership), the profit principle would still be operative. The association would then be operating in the most efficient manner consistent with the conflicting interests of some of its members.

An educational program might permit an association to modify its operations in the future. Differences in members' views toward particular integrating devices may arise wholly because of different interpretations of their effects. But often conflicts arise because some forms of integration affect some members differently than others. For example, some members may find it preferable to grow a lower-quality product (or actually impossible to do otherwise) than is desirable from the viewpoint of the entire

association. For example, there is considerable variation in the size and quality of lemons (and other citrus fruit) grown in different parts of southern California due to a number of factors. Very often there are serious conflicts among the interests of patrons with large and small enterprises. Education is of little help if there are such real conflicts of interests among different members. Often, however, even apparently irreconcilable conflicts of interest among patrons can be reconciled. Quality conflicts, for example, can most often be reconciled by paying on a grade basis and increasing the number of product pools.

Third, not all associations are guided by the principle of maximizing their members' incomes. In some associations a primary objective of the management may be the desire to operate the largest marketing organization in the field—possibly because of a vague notion that market control increases with size. With this as an important objective, associations may shy away from any integrating devices tending to limit membership. This may result in growth at the expense of operating efficiency.

In yet other instances the majority of members of an association may believe that strict integrating procedures are alien to the coöperative way of business.

Finally, some coöperative associations may not use certain integrating devices simply because the managers do not appreciate their importance or their effect on patrons' incomes, or they may be unwilling to require members to subscribe the additional capital for further integration.

Unfortunately, available information does not permit generalizations regarding the importance of the above-mentioned factors in limiting fuller integration of farming operations of patrons with the marketing operations of their coöperatives. But each association should be able to answer this question of integration to its own satisfaction. If it is interested in operating efficiency, it must find an answer. If particular integrating devices promising higher returns are not used, the association should know why. When noneconomic considerations influence an association's decisions, the management should carefully think through such considerations and assess their importance to operating efficiency. Only then can the association know whether it is including the proper integrating provisions in its marketing contracts.

VIII. USE OF MARKETING CONTRACTS BY SUPPLY ASSOCIATIONS

Nine out of ten California coöperatives use marketing contracts, and, as this study has shown, they have sound economic reasons for doing so. Up to this point we have dealt almost exclusively with their use and function by marketing associations. But how about their use by supply coöperatives?

Only one of the eight purchasing (supply) associations in our sample uses a contract. This is a "central" of a federated supply association, which has a five-year contract with its "locals." It is proper to ask why all the other local and centralized purchasing associations do not use contracts with members. For, certainly, if members purchased a high proportion of their needs from their association, it would operate more effectively.

There are two main differences between marketing and supply associations which generally rule out the use of marketing contracts by the latter. First, there is less need for contracts in supply than in marketing associations; second, the objection by patrons to the use of contracts is greater in supply than in marketing associations.

Supply coöperatives involve a looser form of integration than do marketing associations. Few activities of members

and their associations need be integrated. With supply associations, there is nothing comparable to the quality, harvest, and delivery-time integrating requirements so essential to many marketing operations. The only comparable need is that of maintaining volume. But even here supply associations' problems differ. With marketing associations the chief need for total patronage contracts is to protect against short-run threats to performance. (Long-run threats—consistently lower returns—cannot be warded off by contracts.) Contracts are especially important when marketing coöperatives use product pools. For when prices fluctuate from day to day, some members often have an incentive to sell outside their association to benefit from prices temporarily higher than average pool prices. In supply coöperatives this incentive for nonperformance generally is not present, and when it is, it is less important. For one thing, pools are less often used in supply associations. Moreover, supply prices generally fluctuate less than farm-product prices.

But perhaps the chief reason supply associations do not use contracts is that there is strong patronage resentment against them. Potential patrons are unwilling to bind themselves to buy all their supply needs from one association. A single supply coöperative often handles a great diversity of products, ranging from fertilizer and feed to refrigerators and gasoline. Most patrons would consider it entirely unreasonable if their association required them to agree to buy *all* their needs of *all* products supplied by their association. This is much different from marketing associations which customarily handle only one or two products for members and do not require members to give up sovereignty over such a great number of their decisions.

Although none of the local supply associations in our sample use contracts, three deciduous fruit marketing associations also handling orchard supplies do use such a contract for supplies. Their supply business, however, differs from that of the general supply associations in that only a limited line—chiefly fertilizers and orchard sprays—is involved. This is apparently why the members are willing to accept such contracts. Although conversations with the manager of one of these associations indicated that the contracts are not enforced very vigorously, neither are they meaningless, for the association had recently expelled one member for not buying his orchard supplies from it. The penalty for nonperformance in the contracts of these three associations is expulsion; no liquidated damages provision is included.

It should be emphasized that these three associations are exceptions to the rule in California. All the other marketing associations in our sample, which also do a supply business, do not require members to buy from them. This is true of all the citrus and poultry associations, which handle large amounts of supplies for members.

APPENDIX A
Nature of Sample

Much of the general information in this study is based on a questionnaire mailed to 525 California coöperatives. Thirteen questionnaires were returned unclaimed, and we assumed that these coöperatives are no longer in operation. Another 33 associations to which we sent questionnaires were later found to have discontinued operations by 1954. Three concerns reported that they were not coöperatives. After making the above deductions, we have assumed that our universe is made up of 476 California marketing and purchasing associations. This may still somewhat overstate the actual number operating today. The Farmer

Coöperative Service reported 461 coöperatives of all types in California in 1953–54 (Gessner, 1956).

The 228 associations which returned usable questionnaires had a combined membership of 70,200, or about 54 per cent of the membership in all California coöperatives in 1953–54. This estimate is based on the membership of responding centralized coöperatives and locals of federated coöperatives. Actually the number of members is somewhat higher than this because six replying associations did not report the size of their membership. The centralized coöperatives and the federations of local coöperatives from which we received information reported a business volume of about $730 million, or about 63 per cent of the total business of California coöperatives of these types. The centralized coöperatives and the locals affiliated with centralized coöperatives from which we received information reported a business volume of about $445 million, or about 56 per cent of the business of all coöperatives of this type. Thirteen returned questionnaires did not give this information.

The above comparisons of membership and business volume were made by comparing the information received from our sample with the estimates of membership and business volume of California coöperatives made by Gessner (1956).

On the basis of the above comparisons, it appears that our sample of returned questionnaires is somewhat biased in favor of larger associations. For, whereas this sample represents about 48 per cent of all California associations, these respondents have about 54 per cent of the state's coöperative members and handle about 56 per cent of its coöperative business. However, this bias does not seem serious because our sample also includes a high percentage of California's small associations—over 40 per cent.

APPENDIX B

Example of Purchase and Sale Type of Coöperative Marketing Contract

(Headings for the various provisions did not appear on the original contract but have been added by the authors.)

MARKETING CONTRACT

This Agreement, made this day of 19 , between SUN-MAID RAISIN GROWERS OF CALIFORNIA, a non-profit coöperative association organized and existing under the laws of the State of California, hereinafter called Buyer, and hereinafter called Seller.

Witnesseth

1. *Purchase and Sale of Products*

That the Buyer hereby purchases from Seller, and Seller hereby sells to Buyer (except as hereinafter otherwise specified) all of the raisin grapes to be produced during the continuance of this contract commencing with the year 19 , on the following described land in County, California, to wit:

at and for the prices to be paid to the Seller determined as hereinafter set forth.

2. *Requirements regarding production on land other than above*

If Seller shall own or control, or hereafter shall own or control, raisin grapes to be produced during the continuance of this contract on any other land, Seller agrees to sell to Buyer, and Buyer agrees to purchase from Seller, such raisin grapes by executing another contract or contracts therefore similar to this contract, provided, however, that in no event shall this clause require or have the effect of continuing this contract for a period longer than that now or hereafter permitted by law.

3. *Quality and Delivery Time Requirements*

Except as may be otherwise provided in the by-laws of the association, all of said raisin grapes purchased hereunder shall be by the Seller thoroughly and properly dried and cured into raisins, or, in the case of currants, into dried currants, of good color, in original condition, and free from damage of any kind, and after they are cured and made into raisins, or, in the case of currants, into dried currants, shall be delivered upon demand by the Buyer at any time, but not later than December 1st in each year to the receiving station designated by Buyer. Buyer, at its option, may accept delivery tendered after said date, but shall not be required to accept any deliveries after said date, and its failure to accept deliveries after said date shall not release Seller from Seller's obligations to make deliveries as required by this contract. None of said raisins shall be delivered in the form of Bleached raisins.

4. *Form in which Product is Marketed*

Subject to the provisions contained in this paragraph, the Seller shall have the privilege of marketing the whole or any portion of said raisin grapes in any year as fresh grapes for conversion into wine, grape juice or distilled spirits, or for use or consumption in such fresh form, but not otherwise. The privilege herein granted to Seller may be revoked or reinstated by Buyer from year to year by written notice to Seller given in the month of July of each year in which such privilege shall be revoked or reinstated.

5. *Buyer to Establish Grades*

Buyer, on or before October 15 of each year, by resolution of its board of directors, will establish grades for each of the varieties of raisins which are to be handled or dealt with by Buyer, under this contract, and similar contracts executed by other Sellers, including Muscat, Thompson Seedless and Sultana raisins and dried currants, and will determine the standards necessary to be met for each of said grades, and will determine which of said grades in each case shall constitute the standard grade, and will establish a scale of differentials to be paid, not less for the highest grade than one-quarter cent per pound for any Muscat and Thompson Seedless raisins or dried currants, delivered to Buyer which are better than standard grade, and will establish a scale of differentials to be deducted as respects any raisins and dried currants delivered to Buyer which are of less than standard grade.

6. *Payment on Grades and Arbitration of Grade Disputes*

If any of the Muscat or Thompson Seedless raisins or dried currants delivered by Seller to Buyer are better than standard grade, which fact is to be determined by Buyer at the time of delivery thereof, Seller shall be entitled to receive ten days after the time of delivery a bonus per pound for such extra quality Muscat or

Thompson Seedless raisins, or dried currants, equal to the differential established by Buyer as aforesaid for the grade into which the extra quality raisins or dried currants delivered by Seller fall; and if any of said Muscat, Thompson Seedless or Sultana raisins or dried currants delivered by Seller to Buyer are of less than standard grade, proper deduction from the price for standard grade shall be determined at the time of delivery according to the grades and differentials established as hereinbefore set forth, and shall be taken out of the first advance made by Buyer on said delivery. Any dispute as to the bonus to be paid, or the deduction to be made, shall be settled by arbitration. Each party shall appoint one arbitrator and said arbitrators shall jointly select a third and the decision of the majority of said arbitrators shall be binding upon the parties. All expenses of the arbitration shall be borne by the party against whom the decision shall be rendered.

7. *Buyer to Make Advances Ten Days After Delivery*

Ten days after the receipt of said raisins by Buyer at the place mentioned above, Buyer agrees to make to Seller as large an advance per pound therefor as in its judgment financial and market conditions will justify.

8. *Title Passes to Buyer*

This instrument is intended by the parties to pass to and vest in the Buyer a present title and right of possession to all of the crops of raisin grapes covered hereby. The Buyer shall at all times have the right to enter upon said premises and remove the said crops therefrom; but the right of the Buyer to so enter and remove said crops shall not affect the obligation of the Seller to pick, cure and deliver the same as above provided.

9. *Operation Methods of Buyer*

The Buyer agrees properly to process and pack said raisins for the marketing thereof. Any thereof not suitable for marketing as raisins may be marketed for other uses. Buyer, after the processing and packing aforesaid, shall sell the said raisins and dried currants, together with raisins and dried currants received from other Sellers under contracts similar to this contract with which said raisins and dried currants have been pooled, as rapidly as practicable, and for such lawful prices as Buyer may be able to obtain therefor and shall approve, and from time to time, as sufficient proceeds are accumulated, in the judgment of Buyer, to warrant disbursement thereof, shall pay the net proceeds over to the Sellers named in this and similar contracts, according to the quantities and varieties of raisins, or if dried currants according to the quantities and grades thereof, received from the respective Sellers, after deducting:

a. Any advance or advances previously made to Seller; provided, however, that no bonus by this contract agreed to be paid, and paid, to the Seller for extra quality raisins or dried currants shall be regarded as an advance to be deducted as aforesaid;

b. Any deduction which under the terms of this contract is to be made from payments to Seller by reason of the delivery by Seller of raisins or dried currants of less than standard grade;

c. The Seller's pro rata share of all losses and expenses of Buyer incurred in its operations;

d. The deferment for the Buyer's Working Capital Revolving Fund, which, under the terms of the by-laws of Buyer is provided to be deferred from the said payments to Seller and the amount of which deferment shall be determined in accordance

with the terms of the by-laws of Buyer relating thereto, and said deferment shall be credited, handled and dealt with and ultimately paid in accordance with the terms of the by-laws of Buyer relating to said Working Capital Revolving Fund;

e. The deferment for the Buyer's Fixed Capital Revolving Fund to be determined in accordance with the provisions of the by-laws of Buyer relating to its Fixed Capital Revolving Fund, which deferment shall be credited, handled and dealt with and ultimately paid in accordance with the terms of the by-laws of Buyer relating to its Fixed Capital Revolving Fund;

f. Any payments properly chargeable to Seller's account by reason of payments made to discharge liens or encumbrances against the raisins or dried currants delivered to Buyer by Seller and to pay expenses in relation thereto;

g. Any payments properly chargeable to Seller's account by reason of the payment of any orders of Seller accepted by Buyer;

h. Any amounts properly chargeable to Seller's account by reason of any marketing agreement, order, program or plan adopted under any state, federal or other law or by voluntary action of Seller and other growers of raisin grapes or producers of raisins or dried currants whether for expenses of the board, committee or other agency administering such marketing agreement, order, program or plan, or for any other payments or expenses required to be paid or which incurred for Seller's account by reason of such marketing agreement, order, program or plan.

10. *Liquidated Damages for Nondelivery*

The parties hereto fully understanding and admitting that it will be impracticable or extremely difficult to fix the actual damages to the Buyer, which will result from the breach of this contract by the Seller, hereby expressly agree and stipulate that in the event of the Seller's neglect, failure or refusal to deliver to the Buyer the raisins and dried currants purchased hereunder, the Seller will pay to the Buyer the sum of three cents per pound for all raisins and dried currants covered hereby, and so undelivered, as liquidated damages for such breach; any judgment recovered against the Seller in any suit to enforce the contract or any right thereunder to include all costs of court, and all expenses arising out of or caused by the litigation and a reasonable attorney's fee to be fixed by the Court rendering such judgment, and shall be entitled to the benefit of any lien securing any payment hereunder.

11. *Specific Performance and Injunction to Insure Delivery*

The parties hereto agree that in the event of a breach or threatened breach, by either of them of any provision, or covenant hereof, the other party shall be entitled to an injunction to prevent such breach, or further breach hereof and to a decree for specific performance hereof; and the parties agree that this is a contract for the purchase and sale of personal property under special circumstances and conditions; that the Buyer has invested large sums of money in the construction of plants and equipment to carry on its business of processing and packing the products herein mentioned, and is expending and will be compelled to expend, further large sums of money in the operations necessary for the carrying on of its said business, and will yearly enter into contracts for the sale of said products; that Buyer, on account of the character of its operations as a non-profit cooperative association, and its obligations under this and similar contracts, cannot go to the open market and buy raisins to replace any which the Seller may fail to deliver; and that the failure of the Sellers named in this and similar contracts, of which there are several thousand, to deliver such products to the Buyer as therein required will result in irreparable loss to the Buyer.

12. *Pooling of Raisins*

The raisins received under this contract shall be mingled or pooled and sold with other raisins of like variety purchased by the Buyer under contracts similar to this contract. Separate pools of the various varieties of raisins purchased by Buyer under this and similar contracts shall be set up for each crop year and said pools shall be accounted for separately.

13. *Pooling of Currants*

Any dried currants received hereunder shall be mingled or pooled and sold with other dried currants purchased by Buyer under contracts similar to this contract and separate pools of the dried currants purchased by Buyer under this and similar contracts shall be set up for each crop year and said pools shall be accounted for separately.

14. *Method of Payment for Pools*

The amount to be paid to Seller as respects each pool shall be based upon the average price per pound at which all raisins of like variety, or grade if dried currants, in the pool shall be sold. Progress payments, in due proportion, shall be made as respects each pool from time to time as rapidly as in the judgment of Buyer it is practicable to make such payments, and such payments shall be continued from time to time until the accounts of each pool are fully settled.

15. *Relations of Buyers and Sellers under Marketing Agreements*

Anything elsewhere in this contract to the contrary notwithstanding, it is agreed that Seller and Buyer shall comply with any lawful requirements of any marketing agreement, order, program or plan relating to the production, drying, processing, marketing or accounting for the proceeds of the marketing of said raisin grapes, raisins and dried currants heretofore or hereafter adopted or put into effect according to the provisions of any state, federal or other law, and that there shall be set aside and dealt with, as may be required by such marketing agreement, order, program or plan such free, reserve, surplus or other pools as respects said raisin grapes, raisins and dried currants affected by this contract as may be necessary, and that the plan of settlement herein provided for as respects said raisin grapes, raisins and dried currants shall be modified as may be required by such marketing agreement, order, program or plan and as respects such free, reserve, surplus or other pools, and as respects the actions of Seller and Buyer. It is further agreed in this connection that if, when any raisins or dried currants are delivered to Buyer, any marketing agreement, order, program or plan, or any code, license or other action made, adopted, issued or taken under any state, federal or other law shall by its terms or operations require Buyer or Seller to withhold from immediate sale, or to hold for, or deliver to, any board, committee or other agency any part or percentage of such raisin grapes, raisins or dried currants, or to make any payment out of the purchase price or otherwise to any such board, committee or other agency or otherwise, this contract shall be subject to such requirement, and any such withholding, holding, delivery or payment may be done or made by Buyer at Seller's expense and for Seller's account, or as otherwise may be required by law.

16. *Operation under Government Price Programs*

Should the state or federal government fix, or shall have fixed, a maximum price for any raisin grapes, raisins or dried currants agreed to be sold by this contract (a) to be paid to Seller, or (b) to be charged to or by Buyer, or to the jobbing

trade which shall be or represent less than the price otherwise to be paid, then the price otherwise to be paid is to be reduced in case (a) to the price so fixed and in case (b) to a price based on and having a proper relation to the price so fixed. Should the state or federal government limit the quantity of raisin grapes or raisins or dried currants Seller may deliver or Buyer may accept, then the provisions of this contract shall be modified in accordance with such limitations.

17. *Each Portion of Contract is Separate*

Should any portion of this contract be determined to be unlawful, provided that such portion of this contract is severable, it shall be eliminated from this contract and the other provisions of this contract nevertheless shall continue in effect.

18. *Deliveries made in Name of Seller*

All deliveries of said raisins are to be made in the name of the Seller unless notice in writing to the contrary is given to the Buyer by the Seller, and all payments or advances hereunder are to be made to the person in whose name such deliveries are made, or upon orders signed by him and duly accepted by the Buyer; provided, however, that if at the time of such delivery there stands of record a crop mortgage covering the crop so delivered, such payments or advances may be made as directed by request in writing signed by both mortgager and mortgagee, or as otherwise may be required by law. If adverse claims to said payments or advances are made, payment may be withheld pending settlement of such adverse claims without liability for interest or other liability by reason of such withholding.

19. *Termination Rights of Buyer and Seller*

Subject to the limitation of the period of time now or hereafter prescribed by law during which this contract may continue in effect, this contract shall continue in effect until terminated by either of the parties hereto as herein provided. Between December 20 and December 31 of any even numbered year Seller may file with the Buyer a written notice of his desire to withdraw from this contract and thereupon this contract shall be cancelled as to the crops of succeeding years; between February 20 and March 1 of any odd numbered year, Buyer may give written notice to Seller of Buyer's desire to withdraw from this contract and thereupon this contract shall be cancelled as to crops of that and succeeding years; provided, however, that in no event shall this contract continue in effect for a period longer than that now or hereafter permitted by law.

20. *Notices*

The notices herein provided to be given shall be deemed to have been given to the Buyer when mailed to its office in Fresno, California, and to the Seller when mailed to his address as noted hereon.

21. *Succession of Obligation*

This contract shall bind the heirs, administrators, successors or assigns of the respective parties hereto; provided, however, that the same may not be assigned by party of the first part except to a non-profit cooperative association or corporation organized and existing under the laws of the State of California, or any corporation or organization of a cooperative nature which may be authorized by law.

22. *Definition of Raisins and Raisin Grapes*

The terms "raisins" and "raisin grapes" herein shall include the following and

only the following, varieties, to wit: "Thompsons," "Muscats," "Sultanas" and "Currants."

23. *Buyer May Borrow on Pools*

Seller agrees that the association shall have the power to borrow money for any purpose of Buyer on the raisins and dried currants handled by Buyer in any of the pools established by Buyer, or on any other property to which Buyer has title; and that Buyer may exercise any and all other rights of ownership without limitation, and may sell or pledge for its own account or as security for its own debts or otherwise, all or any part of said raisins and dried currants handled by Buyer in any of said pools.

24. *Seller Bound by Articles of Incorporation and By-laws*

Seller, as a member of, or upon becoming a member of Buyer, shall be bound by the provisions of the articles of incorporation, by-laws and rules and regulations of Buyer as now existing, or as hereafter during the life of this contract amended or adopted.

25. *Litigation Costs*

In any litigation between Seller and Buyer, Seller shall pay all costs, premiums for bonds, and other expenses and reasonable attorney's fees as fixed by the Court incurred by Buyer in such litigation, provided that Buyer prevails therein.

26. *Previous Contracts Cancelled*

Any and all crop contracts heretofore entered into by the parties hereto and covering the above described raisin grapes, or any portion thereof, are hereby cancelled as to all crops hereafter to be produced.

27. *Contracts to Incorporate Changes Necessary by Laws*

The parties hereto agree that any modifications of or changes in this contract hereafter required to be made by any state, federal or other law or laws, or by any Court having jurisdiction, shall be deemed to be and are hereby incorporated herein.

28. *Contract is Application for Membership*

The execution of this contract by Seller is also an application by Seller for membership in Buyer and such application shall be deemed to be accepted by Buyer when Buyer shall have executed this contract.

IN WITNESS WHEREOF, the parties hereto have executed this contract as of the day and year first above written.

(Buyer) SUN-MAID RAISIN
GROWERS OF CALIFORNIA

By ....

Witness to Seller's Signature:

....

....

Address

(Seller) ....

Address ....

....

Address ....

APPENDIX C

Example of an Agency Type of Coöperative Marketing Contract

(Headings for the various provisions did not appear on the original contract but have been added by the authors.)

CROP AGENCY AGREEMENT

This Agreement, Made this day of 19 , between CALIFORNIA ALMOND GROWERS EXCHANGE, a corporation hereinafter called the Exchange, and
of hereinafter called the Member.

Witnesseth:

Member to Deliver to Exchange

That for and in consideration of like promises on the part of other members of the Exchange, the Member hereby promises and agrees to harvest, hull, thoroughly dry, clean and deliver to the Exchange at its nearest receiving station, in accordance with the By-Laws and with any and all rules adopted, or that may hereafter be adopted, by the Board of Directors of said Exchange, year by year, and as soon as they can be harvested and prepared for delivery, all of the almonds to be produced during the term of five years beginning on the first day of April 19 , and any extension or extensions thereof on any and all lands now or which may hereafter be owned, leased, operated or controlled by the Member including the following described land in County, California.
(owned, or leased or operated or controlled) by the Member, to-wit:

to be marketed and sold by said Exchange as the agent of the Member.

Exchange Appointed Agent

And the Member hereby appoints the Exchange the sole and exclusive agent of the Member and also as the attorney in fact of the Member, for the said purposes and the purposes hereinafter set forth, with full power and authority in its own name, in the name of the Member, or otherwise to transact such business and take such action as may be necessary, incident, or convenient for the accomplishment thereof, including the power to pool said almonds and to borrow money thereon or upon any of them for the corporate purposes of the Exchange and to pledge, mortgage or hypothecate the same, coupling such appointment with a direct, financial interest as the common agent and attorney of all members hereunder, and without power of revocation, for the full term hereof.

Exchange to Market Crops

The Exchange on its part agrees to prepare for market and to market and sell said almonds as agent of the Member, and to divide the proceeds of the sale of said almonds and of other almonds pooled therewith among its various members at the same rate per pound for like variety and grade and in accordance with the provisions of the By-Laws, after first deducting from said proceeds the expenses,

expenditures and appropriations of the Exchange in doing and performing the things hereby required to be done and performed by it and incidental thereto, or in providing for and carrying on the business, operations and corporate purposes of the Exchange as may from time to time be determined by the Board of Directors thereof in accordance with the By-Laws.

Nonmember Business

The Exchange agrees that during the term of this contract it will not accept for sale or deal in any almonds except for the account of members of the Exchange, and then only under contracts similar in form to this contract, or such other form as heretofore may have been adopted or as in the future may be adopted by the Board of Directors of the Exchange in accordance with its By-Laws, for general use in dealing with its members, provided, however, that in the event of the death of a member, or the termination of the membership of any member, or any other contingency preventing delivery by a member, the Exchange may nevertheless, subject to the limitations of the By-Laws, accept for sale the almonds covered by the crop agency agreement of such member; and further provided that when any almonds grown or delivered to the Exchange by members of the Exchange are insufficient in quantity or quality to meet any unfilled orders held by the Exchange, or when for any other reason the Board of Directors deems it appropriate, the Exchange may purchase, acquire, accept for sale or deal in almonds produced by nonmembers, always provided that almonds grown by nonmembers shall not be dealt in by the Exchange to an amount greater in value than such as are handled by the Exchange for its members.

Liquidated Damages for Nondelivery

The parties hereto, fully understanding and admitting that it will be impracticable, or extremely difficult, to fix the actual damage to the Exchange, which will result from the breach of this contract by the Member, hereby expressly agree and stipulate that in the event of the Member's neglect, failure or refusal to promptly deliver to the Exchange as herein required the almonds which are to be delivered under this contract, or any thereof, the Member will pay to the Exchange the sum of *five cents per pound* for all almonds covered hereby, and not so delivered, as liquidated damages for such breach; any judgment recovered against the member in any suit to enforce this contract or any right thereunder shall include all costs of Court, and all expenses arising out of or caused by the litigation and a reasonable attorney's fee to be fixed by the Court rendering such judgment. The Exchange shall have the right to bring successive actions and recover successive judgments for each neglect, failure or refusal by the member to deliver almonds to the Exchange in accordance with the provisions hereof.

Crop Report

As soon as the fruit has formed upon the trees in each year and whenever thereto requested by the Manager of the Exchange, the Member agrees to mail to the Exchange at its office at Sacramento, an estimate of the yield of almonds covered by this contract, and also, each year immediately upon the harvesting of such almonds to mail to the Exchange a statement of the amount of such yield. (As amended October 21, 1938).

Quality Requirement for Delivery

Should the Member fail to properly harvest, hull, dry or clean the almonds to

be delivered hereunder, or to do any of the things required of the Member hereunder, the Exchange may elect to do what may be necessary in that behalf and may charge the cost thereof to the Member, or may elect to decline acceptance of such almonds, or of almonds in a deteriorated condition or of inferior quality or grade, or almonds otherwise unfit to be pooled with the other almonds handled by the Exchange, or if already delivered, may return them to such Member, at his expense, or may notify the owner thereof and hold the almonds subject to his orders and at his expense.

Specific Performance and Injunctions to Insure Delivery

The parties hereto agree that in the event of a breach or threatened breach by either of them of any provision, or covenant hereof, the other party shall be entitled to an injunction to prevent such breach or further breach hereof and to a decree for specific performance thereof; and the parties agree that this is a contract for the delivery of personal property under special circumstances and conditions; that the Exchange has invested large sums of money in the construction or establishment of plants and equipment to carry on its operations, and is expending, and will be compelled to expend, further large sums of money in the operations necessary to the carrying on of its said business, and will yearly enter into contracts for the sale of said almonds; and that the failure of Members named in this and similar contracts to deliver such products to the Exchange as therein required will result in irreparable loss to the Exchange and to the members thereof.

In consideration of the agreements on the part of the Exchange, the Member agrees that this contract is made for the benefit of, and is beneficial to, the land herein described and/or any other lands now or which may hereafter be owned, leased, operated or controlled by the Member and devoted to the growing of almonds, and to the interest and estate of the Member in such lands, and a lien is hereby created upon all of the said lands and all parts thereof, and the estate and interest of the member therein, in favor of the Exchange to secure payment of all sums becoming due hereunder from the Member and performances of the obligations herein contained upon the part of the Member, which said lien shall continue for the full term of this contract and until such payments have been made and said obligations fully performed, and such lien may be enforced in the same manner as other liens upon property, regardless of the ownership of said lands.

Termination Rights of Exchange

The Exchange may terminate this contract at the end of the contract period above specified by giving to the Member written notice by registered mail of such termination at any time before the end of such period, and the Member may terminate this contract at the end of the contract period above specified by giving to the Exchange written notice by registered mail of such termination at least sixty days before the end of such period, and upon the giving of such notice by either party and the full payment to the Exchange of all just claims and demands, the Exchange shall execute and deliver to the Member or to the owner of the land, a certificate to the effect that such contract has been terminated effective at the expiration of such period, which said certificate shall, at the request and expense of the Member, be acknowledged before a Notary Public so that it may be recorded. In the absence of such notice of termination of this contract by either party as herein provided, it shall continue in full force and effect for a further term of five years with the like right upon the part of either party hereto to terminate it by notice as afore-

said, at the end of such further term. And in the absence of such notice, before the end of said further term of five years, it shall continue in full force and effect for a further term or period of five years. Provided, however, that the Exchange may waive or release the lien herein provided for whenever in the judgment of the Board of Directors of the Exchange such waiver or release may be necessary or proper.

Termination Rights of Members

In addition to the foregoing provisions for termination of this contract, the member may terminate it as of April 1 of any year but in no event as of a date prior to the end of the *second year* of his membership in the Exchange, upon complying with each and all of the following conditions precedent: First, that the member gives the Exchange written notice by registered mail of such termination at least sixty (60) days before such date, second, that prior to the effective date of such notice the member also gives the Exchange as liquidated compensation for any and all loss and expense it may incur or suffer by reason of such withdrawal a written waiver in form and execution satisfactory to the Exchange of any and all rights the member may have to repayment of any and all sums withheld by the Exchange for purposes of the reserves mentioned in Article III of its By-Laws during the contract period or further term of the contract current when the above mentioned notice is given and not payable or for which a date for payment prior to the effective date of said termination shall not have been fixed prior to the giving of said notice as well as of any and all rights the member may have to interest on account of the money in said reserves unpaid at the time of the giving of said notice, and in addition if any amount of the member's share of any or all of the aforesaid reserves has been made the subject of an assignment whether voluntary or by operation of law which the Exchange has recognized or is entitled to recognize, furnishes the Exchange evidence satisfactory to it that a complete reassignment to him has been made or in the alternative pays to the Exchange the amount so assigned together with the amount of any interest payable on account of the amount so assigned for the interest period current when such notice is given, and, third, that prior to or on the effective date of the notice of termination the member pays to the Exchange the full amount of all just claims and demands which it may have against him. The liquidated compensation aforesaid shall be applied against the expenses of the Exchange for the crop for the calendar year in which the termination becomes effective or in the event the Exchange should be dissolved without handling such crop, then against the expenses for the last crop handled by the Exchange. Upon the member's complete compliance with the foregoing provisions and not otherwise the Exchange shall execute and deliver to the member or to the owner of the land a certificate that said contract has been terminated as of the effective date of said notice of termination which certificate shall, at the request and expense of the member, be acknowledged before a Notary Public so that it may be recorded.

Termination Upon Dissolution

In addition to the foregoing provisions for termination of this contract, the Exchange may terminate this contract on the first day of April of any year in the event that at least two-thirds of the members shall have theretofore voted for dissolution of the Exchange, such termination to be effective by giving to the Member written notice thereof by registered mail.

Noice of Termination

Notice of the termination of this contract or any extension thereof upon the part of the Member shall be deemed to include and constitute notice of termination of membership under Article XI of the By-Laws of the Exchange.

Miscellaneous

The Member hereby acknowledges receipt of a copy of the By-Laws of the Exchange and assents thereto and agrees to be bound thereby and by any amendment thereto adopted as provided in Article XV thereof.

This contract shall bind the heirs, executors, administrators, successors, assigns or grantees of the respective parties hereto; provided, however, that the same may not be assigned by the Exchange except to a non-profit, co-operative association organized and existing under the laws of the State of California, or a corporation or organization of a co-operative nature which may be authorized by law.

It is agreed that this contract contains the whole agreement between the contracting parties and no statements or representations are of any force or effect unless set forth herein.

CALIFORNIA ALMOND GROWERS EXCHANGE

By ....

Secretary

Sign Here ....

WITNESS to Member's Signature:

Address ....

....

....

Address ....

....

Address ....

I, the undersigned, having an interest in the above mentioned lands and crops, hereby consent to and join in the execution of the foregoing contract, and agree that such interest shall be fully bound by and subordinated to said contract. In the event the right of possession of the above named grower in or to such lands or crops may be terminated with resulting reversion to me, I shall be bound by said contract during the remainder of the term thereof. I further agree that any transfer I may make of my interest in said lands and crops shall be made subject to said contract.

....

WITNESS to Signature:

Address ....

....

LITERATURE CITED

BAKKEN, HENRY F., and MARVIN A. SCHAARS
1937. The economics of cooperative marketing. New York: McGraw-Hill Book Co. 583 p.

COCHRANE, W. W., and R. H. ELSWORTH
1943. Farmers cooperative discontinuances. Wash., D.C.: U. S. Farm Credit Admin. Misc. Rept. 65.

GARDNER, KELSEY F., and A. W. MCKAY
1950. The California fruit growers exchange system. Wash., D.C.: U. S. Farm Credit Admin. Cir. C-135.

GESSNER, ANNE L.
1957. Statistics of farmer cooperatives, 1954–55. U. S. Department of Agriculture, Farmer Cooperative Service Gen. Rpt. 23.

HOOD, ROBIN
1927. Liberalizing the members' contracts. Cooperative Marketing Journal 1:287–293.

HULBERT, L. S.
1942. Legal phases of cooperative associations. Wash., D.C.: U. S. Farm Credit Admin., Cooperative and Service Division Bul. 50.

JESNESS, O. B.
1923. The cooperative marketing of farm products. Philadelphia: J. B. Lippincott, 292 p.

JOHNSON, GEORGE F.
1924. The cooperative marketing contract. Wisconsin Agr. Exp. Sta. (Processed)

MACCURDY, RAHNO M.
1925. The history of the California fruit growers exchange. Los Angeles: G. Rice and Sons, printers. 106 p.

NOURSE, EDWIN G.
1927. The legal status of agricultural cooperatives. New York: The Macmillan Co. 555 p.

PACKEL, ISRAEL
1947. The law of the organization and operation of cooperatives (2d ed.). Albany: Matthew-Bender and Co. 389 p.

PHILLIPS, RICHARD
1952. Economic nature of the cooperative association. Unpublished doctoral dissertation. Iowa State College, Ames, Iowa.

STEEN, HERMAN
1923. Cooperative marketing. New York: Doubleday-Page. 366 p.

In order that the information in our publications may be more intelligible it is sometimes necessary to use trade names of products or equipment rather than complicated descriptive or chemical identifications. In so doing it is unavoidable in some cases that similar products which are on the market under other trade names may not be cited. No endorsement of named products is intended nor is criticism implied of similar products which are not mentioned.

7½m-3,'58(332)BEB

141